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*Friends-of-the-Firm Briefing*

# So You Want To Start Your First New Company?

## *24 Critical Business Principles That Even Seasoned Entrepreneurs Forget*

By Alan G. Dunn, President
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*GDI Consulting & Training Company provides practical solutions to complex business and managerial problems. Focusing mainly on the manufacturing and distribution industries, GDI has developed a reputation as one of the most innovative and hardest working professional services firms in these industries.*

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## *Forward by Alan G. Dunn*

Dear Friends-of-the-Firm,

Many years ago I started my first company. Fortunately, I started it with the wisdom of an experienced partner, more than twice my age, which helped guide me through many of the typical difficulties of the new venture. He was not only a Board member, but also a friend who taught me that business is more than just a great product in a great market. Most of all he taught me that the people who would eventually work for me would ultimately determine my new venture's success or failure.

This Friends-of-the-Firm briefing is a compendium of lessons I have learned from entrepreneurs who, like me, started, succeeded and sometimes failed in their business ventures. Many of them have become close friends and confidants who have been kind enough to share their key lessons learned from their successes as well as their mistakes. This briefing summarizes those lessons that seemed to me and my colleagues to be the most important and inspirational lessons. I sincerely hope that these often forgotten lessons will help you learn from others actions… at a much lower price!

When I think of my business ventures in the context of these lessons, I am struck by how easy it is to talk about lessons and how difficult it is to inculcate them into one's personal business constitution. I am certain that those who provide these bits of advice are also talking to themselves… using these words as a reminder as much as a lesson plan. It seems it is still easier to teach than to do!

Attempting to follow these principles has become an obsession with many of my clients. I am proud to say that those who actually practice these principles appear to be creating wealth at a faster clip than those who don't pay attention. Perhaps these principles will strike a cord with you and help you in your first (or next) business venture like they have for many of my clients.

Happy reading.

Alan G. Dunn
President
GDI Consulting & Training Company

# So You Want To Start Your First New Company?

*By Alan G. Dunn*

There is probably not a human being in the free world that has not at one time thought of starting his or her own business. Though there is no scientific or empirical proof, it seems as though human beings long to be their own boss, set their own direction and create their own future. This inevitably leads to contemplation of a new business venture with the thinker as the creator and leader.

If you want to start a new business, you will have to follow several principles that have been around as long as people have contemplated the development of new business ventures. Though most of these principles represent sound application of common sense, many are less than intuitive and most require practice in order to make them routine. Following them will be a fundamental part of starting your new business and, though not guaranteeing you success, will assuredly stack the odds in your favor. If you do not follow these principles, you are sure to go broke - both financially and emotionally.

The principles discussed in this article are not to be considered in any priority sequence. All are important. All are to be contemplated and all are to be practiced in a routine fashion during the start-up phase of your new business venture. Most importantly, all of the principles apply to all types of business - from development and marketing of high technology weaponry to the start-up of a "mom and pop" gift shop. These fundamental principles are as follows:

1. **Never get emotionally attached to your business.** Businesses are designed to start, grow, enjoy and even sell. Entrepreneurs who start a company, build it and then watch it die while turning away offers to sell the company, often end up losing their total financial and emotional security base. Do not get so emotionally attached to your business that you loose objectivity and view it as anything other then something that generates wealth for the stockholders (which hopefully will be you).

2. **Treat your company as an experiment.** This is particularly true in your first company if you are one who will develop several in your lifetime. If you treat your company as your “experiment” instead of your “baby”, you can never fail. If the company does not perform, your experiment has provided you with information regarding what not to do, which of course, will be very helpful in your second venture. Many successful entrepreneurs have one or more business collapses in their background. The reason they eventually become successful is that they have personally experienced the trauma of the events that lead to business collapse. Having experienced this, they can than predict trauma faster and take corrective action sooner. Treat your company as an experiment in what is right, be willing to make a mistake and make adjustments to the experiment when necessary. If all else fails, cancel the experiment and start again!

3. **In the early phases of your company's life, ignore profit and loss statements and balance sheets.** Instead, concentrate on cash flow and liquidity. It is a good idea to run your start-up company on a "month of expense coverage" basis. This means that you estimate the cost of running your company on a monthly basis and reserve liquid assets (usually cash) to cover all of these expenses for X number of months. Depending upon the industry, X number of months can vary. Rules of thumb for month of expense coverage to receive in the form of liquidity are as follows:

   - 6 months of expense coverage for service firms.
   - 4 to 6 months expense coverage for retail operations.
   - 6 or more months of expense coverage for manufacturing operations.

   Keeping several months worth of liquid assets provides you with a cushion in case of downturns in your business. This effectively reduces the risk of being in business and keeps you from negotiating quality when times get tough. Let your accountants worry about profit and loss and the net worth of the company. You worry about paying the bills and creating the cash that is necessary to run the day-to-day operations. Cash flow management is the name of the game in the early stages of your company!

4. **Develop a formally written strategic business plan.** Be sure to discuss the products and services your firm will develop and provide. Also, be sure to define in detail how you will reach your marketplace. This includes analysis of advertising, promotion, public relations and distribution channels. You should also analyze the financial issues, the design, development and overall business strategy issues. In other words, get a book on strategic business planning, write a strategic business plan and live by it! Do not think you can do it on the back of a napkin and do not think it is an informal and unnecessary procedure. Writing it down will give you guidelines to think about as your company grows and the opportunity to expand as your net worth increases. In many companies, the business plan also provides information which helps keep the people focused and away from the "wandering opportunity syndrome."

5. **There is no substitute for getting good legal and accounting advice when you start a company.** You should talk your idea over with a lawyer and an accountant and make sure there are no liabilities, contingencies or particular accounting issues that should be discussed in the early phases. This does not mean you should allow your lawyer or accountant to judge the merits of your idea. Generally speaking, lawyers and accountants are rotten business people who cannot tell the difference between a good business idea and a bad one. If they could, they would most certainly be in a different line of business! They can, however, keep you out of trouble with your competitor, the government and the Internal Revenue Service… using them wisely in the early stage of your start-up venture will save you many thousands of dollars (maybe even millions!) as your company matures.

6. **Get yourself a "confidant".** Find somebody to talk to. The problem with entrepreneurs is that they can't talk to anybody. If they are fortunate enough to have a good board of directors, sharing with the board could be disastrous. Entrepreneurs are idea-oriented

individuals. Those who work around them often consider them "nutty". Sharing "nutty" ideas with a board of directors can result in you looking for a new board under unfavorable circumstances. Talking to your employees can be equally disastrous because they may actually interpret your idea as direction and begin executing it! Get yourself a confidant outside the company who is willing to listen and talk very frankly, but emphatically, with you. Of all the suggestions for new entrepreneurs, this is one of the most important.

7. **Establish control systems for managing cash and all that affects cash the first six months of the business.** If you are successful, you will not have time to establish these at a later date when cash will be in short supply. Control of cash is tantamount to survival in an entrepreneurial start-up venture. If you cannot sign every check and see every dollar in and every dollar out, you must establish non-parochial and non-bureaucratic systems that will ensure that cash is being managed properly. Develop these in the early stages of the company and you will pay less bank penalties, miss fewer payments to critical vendors and never find yourself up short cash when you least expect it. It really is okay for the President of a million dollar company to sign every check!

8. **Don't get carried away with technological solutions to managerial, procedural and marketing problems.** These days, entrepreneurs want to use computers to solve all of their problems. The bulk of your problems in a start-up environment have nothing to do with computers. They primarily revolve around getting enough capital to run the business and finding enough customers to buy the products. The equation is not all that complex. It just gets muddled when entrepreneurial priorities concern themselves with other than marketing and production processes. Concentrate first on the fundamentals. Master the fundamentals and then look at technological devices!

9. **Learn to set priorities.** Generally speaking the priorities of a new venture (after initial start-up) are as follows:

   - First and most importantly is to find innovative ways of getting customer orders for your product or service. This does not mean shipping the order. It only means finding ways of getting the order.
   - Find enough money to support the organization in order to get the order out the door.
   - Develop the processes and mechanisms for making the product or delivering the service.
   - Develop the mechanism or processes to make sure that (administratively) your organization runs routinely.

10. **It is critical that your operation run itself as soon as possible.** Entrepreneurs tend to be good in a few disciplines. In the early stages of business development, their talents are most needed in the discipline they enjoy. Later however, the entrepreneur may have to apply different sets of talents in areas the entrepreneur does not like working within. This, of course, signals a certain maturing of the organization. The rule for successful entrepreneurs, though frequently violated, is: *"Do not work when you want to work.*

*Work when the company needs you to work. Recognize on the outset that the "need" will change every year! Be prepared to change your personal focus every year".*

**11. All "entrepreneurs in training" must condition their physical being for entrepreneurship.** If you are not actively participating in an entrepreneurial role at this time, you should begin your training immediately. Start by learning how to wake up every morning at 5:00 AM, be at work by 6:00 AM and leave work at 11:00 PM. Also, learn how to work on many tasks at the same time, change your personal schedule dramatically on a moments notice and work intensively This last item means getting more work done in an hour then you ever previously got done in an hour. Intensity, strength of work ethics and willingness to put in long hours, are always a prerequisite of the entrepreneur. Most importantly however, you must not only work hard and long, you must actually <u>enjoy doing it!</u> If you do not enjoy doing it, you will get burned out very quickly.

**12. Pay yourself.** First make sure your company's monthly expense budget includes a <u>salary</u> to you. The general rule of thumb when using limited amounts of cash are as follows:

- Pay your employees first.
- Pay Uncle Sam second.
- Pay those who can shut you down or those who are unwilling to negotiate third.
- Pay yourself fourth.
- Pay your remaining vendors last.

If you cannot afford to pay yourself, you will not be in business very long. Do not take a portion of profits out of the business when those profits exist. Pay yourself a monthly salary (commensurate with the company's revenue stream) and let the remaining cash accumulate for later use in operations. Make sure that your salary is considered part of the monthly expense budget!

**13. Never mortgage the roof over your head.** As a start-up business, banks and financial institutions will want you to collateralize their loans with your personal assets. Never do this, because if you go out of business, you will be wiped out both <u>personally and corporately</u>! Any bank which requests an entrepreneur of a start-up venture to put up personal assets as collateral should be shown the door… quickly! Keep your business activities a business and your personal life personal. Never let the two mix… at least financially.

**14. Lecture your employees at least once a month about the necessity to control cost.** Make the concern for cost control an "institution" within your company. If you wait until the company grows, it will be virtually impossible to establish a culture of cost management in your organization. Start your company assuming you will be successful and begin establishing cultures, systems and institutions to help you carry out the success.

**15. Learn the business before you start the business.** If you are going to start a dental practice go to work for another dentist and learn the "mechanics" of being in the dental business. Learn what makes others successful and learn what makes them fail. Above all, learn all you can about the day-to-day problems and issues of the industry. If you already work in the industry that you plan to compete, go to work for <u>another</u> company. Get as many perspectives as possible before starting your company. Get your education at some else's expense!

16. **Set expectations higher than your competition.** As the new kid on the block, you will have to work harder, smarter, longer, more intensively and with less short-term rewards than do your competitor. Set expectations high and stick to the - even if you experience higher than expected employee turnover. If average is considered 70%, you must consider it 85%! Set the minimum standards expected for your people high and challenge them on a regular basis. You do not have time to employ "touchy - feely" or participative -management techniques every day. You must move faster and more aggressively than your established competitor if you are to survive. Plead with your employees on a regular basis - tell them of the "little guy" plight and solicit their help. It is a fact… most people like being driven so long as the drive is exciting and the potential outcome is possible. Your people will help so long as you direct them in a "firm but fair" manner and communicate regularly with them. They may even overlook some of your foibles and idiosyncrasies

17. **Leverage EVERYONE'S pay!** If possible, tie at least one-third of every employee salary to company and personal performance. From the outset, establish a "performance pays" culture in your company. You will not be able to easily implement a performance payroll type compensation package once your company matures. Start it early and you will save money while at the same time, preparing for the future.

18. **Use other peoples' money when ever possible**. You can use other's money by either borrowing or selling a part of the business. Both have their advantages and disadvantages. Both however are ways of financing your company's growth without using significant sums of your own friends. Be careful in your selection of financing, but work hard to share the financial risk.

19. **Have a Buy/Sell agreement between you and your partner.** Regardless of business form (Corporate, Partnership, Sub Chapter S Corporation) you must plan for a future "ownership breakup." Do not assume that you and your partner will always be in business together. A multitude of pressures and business variables constantly work to drive partners apart and eventually and quite frequently force a "dividing up" of the business. Personality clashes, business style differences, economic conditions, company performance, family problems and dozen of other variables inevitably test the business partners relationship and ability to work together harmoniously. These pressures sometime become so severe, that they have been aggregately described as the "Devil" of business partners. When starting your business, create a formal contract that clearly define the terms of separation should the "Devil" get the better of you. Minimum conditions to define include:

    - How the business will be shared upon a splitting up of the owners.

    - How payment to the leaving party will be made and when it will be tended.

- The conditions for termination of one or more partners.
- Legal responsibilities for all partners.

Don't assume that because you and your partners are childhood best friends that a break-up will never occur. Treat each other like business partners only, when starting your business.

**20.** **Someone must have the last and decisive word.** Companies which are run by committee or majority vote almost always fail because they can't move at a "competitive speed". Decide who is in charge and let him or her run the company. Do not rule by consensus during the early stage of company life!

**21.** **Be willing to directly and clearly tell employees what to do.** Great leaders do not buy into pure consensus when determining what direction to take. Consensus is for determining how to do things. Owners are, by default, leaders. They must be clear and decisive and not get caught up in all of the pseudo intellectual culture-babble promoted in business books written by those who have never experienced the need to make a payroll!

**22.** **Establish a "Projection Mentality."** Learn to perform sales, cost and margin forecasts every month, at the same time and in the same place. Establish a culture which seeks to predict a crisis before it happens instead of always reacting after the manifestation of a crisis. You should update your HONEST revenue and cost (expense) projection every month and take corrective action immediately. Do not shy away from tough decisions. Look forward to them and move on them!

**23.** **Do not avoid or delay in dismissing sub-standard employees.** You should not permit a non-performing or low performing employee to work for you, even if it is distasteful to dismiss the employee. Companies that let sub-standard employees continue their employment earn a quick reputation as a lethargic and poorly managed operation. This makes it harder to attract good talent when you need them most… in your companies early days! Promote the achievers and dismiss the non-achievers… regardless of effort! In your company's early phase you should only employ those who can achieve results.

**24.** Finally, **concentrate on doing what is right even if it isn't popular.** As an entrepreneur you will learn first handed the definition of compromise. But, be careful about compromising on important issues just to be liked or because the decision will be popular. Always do what is right irrespective of its popularity. This will manifest itself in a "Firm - But - Fair" management style that may end up being a cultured element in your company. When all is said, your employee should say about you, "I don't necessarily like him/her, but I know he/she believes that his/her actions are in the best interest of the company". Attitudes like this may not get you invited to the social event of the season, but it will gain the loyalty, respect and trust of your employees. And remember, employees always follow those whom they respect, though they may not follow those whom they like. Be willing to make the tough decisions quickly!

If you follow these basic principles of business, you cannot fail. If your company does not achieve your projected financial and emotional results, you will either discover it and initiate corrective actions, or will use the information in your second venture. In either case, the education you have received by starting your own company and following these fundamentals is one that even the Harvard Business School cannot teach effectively.

# About the Author

Alan G. Dunn is currently President of GDI Consulting & Training Company and founder of the Manufacturing Executive Institute (MEI). He is also the creator and lead-instructor of the 18-month Next Generation Global Supply Chain Leadership Development Program at the California Institute of Technology's (Caltech) Center for Technology & Management Education (CTME), where he has taught since 1984. Mr. Dunn also serves on the University of California at Riverside's (UCR) Advisory Board for Transformative Leadership in Disruptive Times.

Mr. Dunn specializes in supply chain management, strategic planning, manufacturing management, operations management, leadership development, cost management and business finance.

Previously, Mr. Dunn was a Vice President at Gemini Management Consulting and a Partner at Coopers & Lybrand. In both positions, he led large technical manufacturing teams through innovative productivity enhancement projects. Mr. Dunn has participated in >188 significant manufacturing and distribution projects inside >118 companies. He has worked in 24 countries and across most manufacturing sectors.

Over his 40-year career in global supply chain consulting, Mr. Dunn has served on the Boards of Directors of numerous public, private and non-profit companies. He is the recipient of the National Association of Corporate Directors (NACD) prestigious *"Director of the Year"* award in 2007.

Alan is a career Association of Supply Chain Management (ASCM) volunteer, having served as the President of the Orange County Chapter in 1984 and Chairman of ASCM in 2015. He was inducted into the *"ASCM New England Supply Chain Conference Hall of Fame"* in 2022.

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