

13 The operational plan

OBJECTIVES

To explain how the business will actually carry out its activity, an operational plan is required. The operational plan is central to the allocation of resources. It uses inputs from the marketing plan to scale operations in order to deliver what is set out in the marketing plan, and it includes information about all stages of primary value chain activities as well as support activities.

The operational plan should contain a description of the organisational structure, including an organisation chart. Human resources are one of the most important resources of a business, and payroll and related costs account for a large part of operational expenditure.

In the context of business modelling, the operational plan is a spreadsheet model which includes most operational and capital expenditure items and the quantification of physical items, such as office space, plant and machinery. The operational plan is the main cost driver, whereas the marketing plan (see Chapter 11) is the revenue driver. It includes the cost of sales and some marketing costs.

LEGAL FORM OF BUSINESS AND OTHER FORMALITIES

One of the first steps is to decide the legal form of the business: sole trader, partnership, limited liability partnership, limited company, or another corporate form that may be available in different jurisdictions. The legal form should be appropriate to the business in question, its future expansion and capital structure.

The legal form of the business is also important in terms of control and corporate governance. The relationships between investors can be further refined by means of shareholder agreements or specific clauses in the articles of association.

Among the formalities that should be addressed are the following:

- Company formation
- Location of registered office
- Appointment of accountant and auditor
- Appointment of company secretary
- Registration of business in commercial register or chamber of commerce
- Membership of industry associations
- Registration with the tax authorities
- VAT registration
- Registration of internet domain name
- Establishment of company bank account and payment facilities
- Registration of trade marks

It is important to be aware that in some countries, such as the UK and the United States, a business can be set up quickly (often in one day) and cheaply, but in others the process can take up to two months and may involve a great deal of form filling, authorisations, certified translations, notarised documents, fees, and so on.

ORGANISATIONAL STRUCTURE

The organisational structure itself should be consistent with the vision and objectives of the business and can be a source of competitive advantage. The organisation chart should reflect responsibilities for delivering margin and take account of the elements of the value chain. It identifies the departments, lines of reporting, span of control and staff numbers. Departments reflect the specialist skills that are necessary to deliver value to the customer. Reporting lines identify responsibilities, power and information flow. The number of subordinates directly controlled by a manager or supervisor is referred to as span of control. Particularly in larger organisations, management layers are an important cost factor. There should be a balance between what managers can achieve without being overburdened and the desire for a lean organisational structure.

Types of organisational structures

The structure of an organisation will depend on size, geographic scope and type of industry.

Functional structure

A functional organisational structure divides the business along the main value chain activities, with each function reporting to the top management. This type of structure is simple and provides clear reporting lines. It is suitable for small companies because people can communicate easily and are usually aware of what other departments are doing. In very small firms, one individual may carry out several functions, but the functional positions should be identified. For example, an inventor who founded a business may be the chief executive officer and the chief technical officer.

Divisional structure

A divisional structure is suitable for larger companies. The divisions may be strategic business units (SBUs), which can be extremely diverse with very different products and markets. The structure must be tailored to meet the needs of each SBU. Some functions, notably support functions of the value chain such as finance, human resources, and research and development, may be located at head-office level.

Decisions on whether to locate particular support functions at head-office or divisional level depend on the diversity of the SBUs and the benefits of centralisation compared with decentralisation. The more decentralised an organisation is, the easier it is to apply a product-portfolio approach to strategy development. However, decentralisation may also imply duplication and the inability to exploit cross-divisional synergies.

A divisional structure may be particularly appropriate where the SBUs are also physically separate, for example located at different sites or even in different countries. It may be necessary for legal reasons to operate an SBU in another country as a subsidiary rather than as a branch office. Where businesses are located on different continents, differences in time zone, language and culture may necessitate a division along geographic lines, but some functions, such as R&D, may still be centralised.

Holding company structure

A holding company is a small unit controlling a collection of independent companies which may not even be wholly owned subsidiaries. The holding-company functions are reduced to a few support functions such as finance and overall strategic planning.

Matrix structure

The matrix structure combines elements of the functional and divisional structure. The value chain and the marketing view of business (see Chapter 11, Chart 11.1, on page 99) both require a product-oriented structure. If a product manager is responsible for delivering margin, he or she must have some influence across all primary activities. The manager has to ensure that the value chain is optimally configured and resourced to support the chosen product strategy.

However, primary and support functions are a shared resource among several products. For example, a telephony company may have a consumer and business telephony product because the needs of the segments are very different. But the network over which services are delivered (switches, transmission and so on) is the same, and there has to be one person responsible for network operations.

The dichotomy of the product-management approach and functional organisation is resolved by adopting a matrix organisational structure. A matrix structure is more complex and requires more management interaction. Conflicts can arise if reporting structures or responsibilities are not clear. In the case of the telephony company, the quality of service the business product manager requires may be different from what the consumer product manager requires, but this cannot be provided because the network is the same. There has to be a final arbiter who is hierarchically above the product managers, but the responsibility of delivering margin for a product always stays with the product managers.

Chart 13.1 **Functional structure**

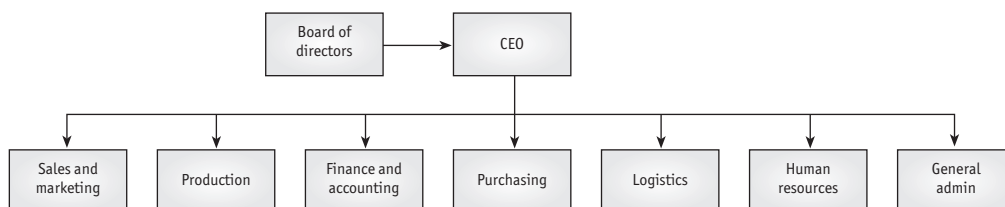


Chart 13.2 Divisional structure

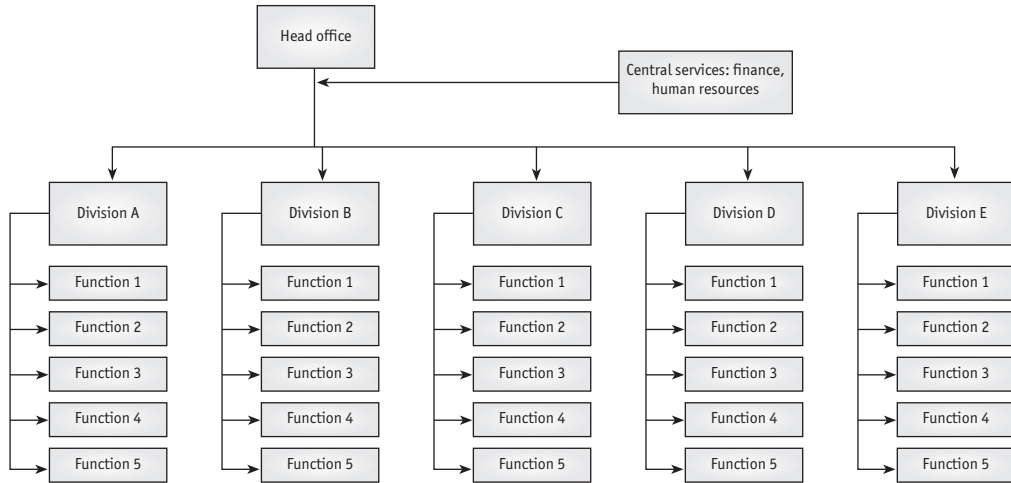
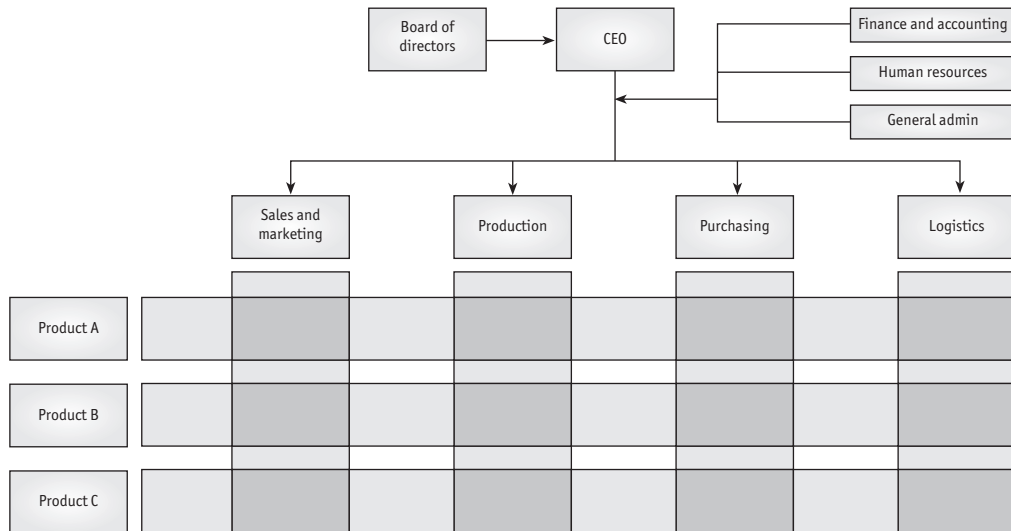


Chart 13.3 Matrix structure



The management team and corporate governance

It is important, particularly for new businesses, to demonstrate that a management team with the right skills is in place. A new investment is a bet on the future where the odds are substantially improved if the business is run by managers who can not only execute the plan but also respond flexibly to changes in the environment as they arise. Board directors (including non-executive directors), top management and key functional managers must be identified by name. Their cvs should be in the appendix to the business plan.

The functioning of the board should be described and the role of the chairman compared with the managing director or CEO should be explained. If appropriate, make reference to guidelines of corporate governance and explain how shareholders exercise control of the board.

HUMAN RESOURCE MANAGEMENT

Having identified and described the management team, the next step is to address staffing. This includes staff numbers, recruitment, retention, training and redundancy. These factors will be a major driver of operational costs. The costs are not just salary and related costs such as employer's contribution to insurance, pensions and training, but also office space, workstations and other items.

Human resource issues to be addressed in the business plan include:

- Appropriate staffing to cover shifts, holidays, illness.
- Span of control, that is, how many managers per staff.
- Salary levels.
- Are trained staff available or do staff have to be trained.
- Continuing training.
- Recruitment costs.
- Staff turnover.
- Employment legislation (working hours, work environment, health and safety, pensions, redundancy).

PHYSICAL INFRASTRUCTURE

Investors want to know what their money is being spent on, so the business plan must identify and describe the physical infrastructure of the firm. The infrastructure comprises all major assets, new assets that have to be acquired, and their function and physical location. Such assets include office space, production facilities, IT and support systems, vehicles and any other facility used by the organisation.

If factories are to be built, the sites should be identified. The reasons for location at a particular site should be explained, for example the price of land, the availability of transport links, nearby qualified staff, or government grants.

Facilities can be bought (capital expenditure) or rented (operational expenditure). Either way, the physical infrastructure is a major cost driver and deserves appropriate attention. Rent or buy decisions should be based on careful analysis of the financial implications, looking at funding, profitability, tax and liability issues. For example, long leases create a liability to pay future rents, whereas loans can be secured against a building that is owned outright.

In some cases, the business plan must include a detailed technical description of the facilities. For example, if a new telecommunications network investment is considered there must be a network plan with all relevant elements identified and costed. For a manufacturing business, the processes and required machinery should be described. Depending on the relative capital intensity of a firm, the description of fixed assets and how they are financed will be more or less detailed.

CAPITAL AND OPERATIONAL EXPENDITURE

The operational plan drives capital expenditure (capex) and operational expenditure (opex). The business plan modelling of these is discussed in Chapter 14. The manner in which opex and capex are modelled should reflect the organisational structure. This will make it easier to understand the link between the financials and operations. In practical terms, this could mean organising the spreadsheet business planning model along departmental lines. There could be one worksheet per department, showing clearly that the budgetary responsibility lies with the relevant departmental manager, who is also identified on the organisation chart.

The linkage between organisational structure and financials makes it possible to identify the cost of particular activities. As a result, the profitability of SBUS or products can be ascertained not just at gross margin level (see Chapter 11) but also at EBIT (earnings before interest and tax) level.

You may even go further and identify the cost of value chain activities. An understanding of costs is as important as understanding revenue, for without knowing costs it is impossible to identify where value is added. In mature markets, an understanding of costs and how to trim them is of pre-eminent importance.

USES OF OUTCOMES IN THE BUSINESS PLAN

The operational plan explains how the business is structured, what resources are required and how these resources are employed to achieve the strategic objectives. It explains how investors' money is spent. In financial terms, it provides most operational expenditure items and all capital expenditure items as inputs into the business planning model.

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