

GSBI SOCIAL BUSINESS PLAN PARADIGM

- Mission/Opportunity/Strategies
- External Environment Analysis
- Beneficiary (“Market”) Analysis
- Operations and Value Chain Analysis
- Organization and Human Resources
- **Business Model, Unit Economics, and Financial Plan**
- Metrics and Accountability
- Operating Plan and Budget
- Financing

Business Model

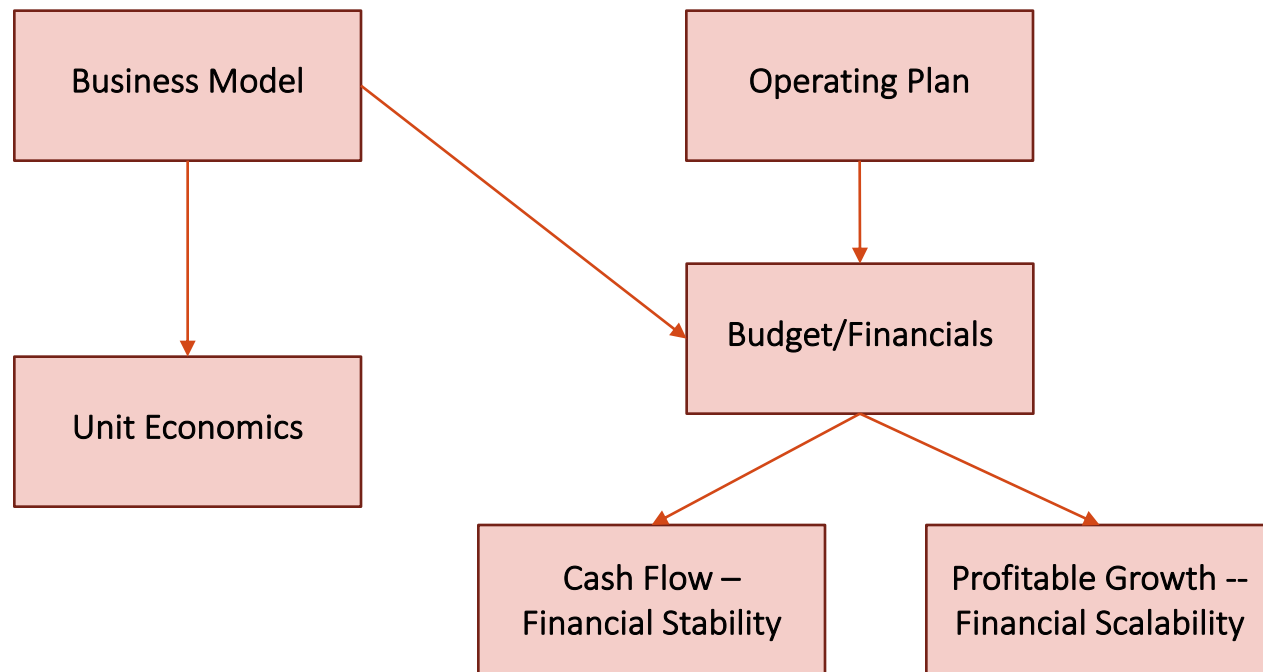
Readings

- Richard G. Hamermesh, Paul W. Marshall, and Taz Pirohamed, “Note on Business Model Analysis for the Entrepreneur,” *Harvard Business School Report* 9-802-048, January 22, 2002.
- *Carlson and Koch* Chapter 9

Business Model and Financial Plan Topics

- Business Model: What and Why Important
- Financial Sustainability/Scalability
- Business Model: Definition
 - Value Proposition
 - Income Drivers
 - Expense Drivers
 - Cash Flow/Requirements
 - Critical Success Factors
- Unit Economics
- The Financial Plan
- Report #6

Business Model: Basis for Financial Sustainability/Scalability, Unit Economics, and the Financial Plan



What is a “Business Model”?

- Sometimes defined by the “legal” organization structure (for taxation).
 - Profit
 - Non-profit
 - Hybrid (non-profit + profit)
- Sometimes defined by what the organization produces.
 - Product
 - Service
- Sometimes defined by the organization's mission.
 - Financial
 - Social
- Sometimes defined by the organization's income statement.
 - Income
 - Expenses
- Sometimes defined by the organization's value chain
 - Operations (manufacturing, microfinance, ...)

Why is a “Business Model” Important for a Social Business?

- Focus the organization on the key activities to create value for the beneficiaries.
- Manage cash in order to create value sustainably.
- Identify and test key assumptions (critical success factors) on which the value creation is based.
- Present (“sell”) the organization (e.g. to investors, partners, employees)

Value

Social and Economic Dimensions

- Social Benefit Definition of Value:
 - Improvement in well-being . . . *life choices* of beneficiary . . . *outcomes and impact*—including environmental sustainability
- Economic Definition of Value:
 - Beneficiary/customer is willing to pay
 - Economic buyer may be a third party

The Business Model “Top Line” For-profit/Not for Profit/Hybrid

- For-profit (Financial ROI Business)
 - A central part of your mission is financial return for your investors (dividends, interest, share price)
- Not for profit (Social ROI Business)
 - Your mission is based on social (impact) return for your investors
 - Surplus income is “reinvested in the business” (not returned to investors)
- Hybrid
 - Multiple (usually two) organizations (for-profit and not-for-profit)

The Business Model “Bottom Line” Sustainability/Scalability

- Sustainable Value Creation
 - Annual surplus income (total income > total expenses)

POSITIVE CASH FLOW

- Scalable Value Creation
 - Sustainable (annual surplus income)
 - Surplus income and expense growth drives
 - Beneficiary/Impact/Value growth
 - B/I/V growth drives income growth

INCOME AND IMPACT GROW FASTER THAN EXPENSES

Business Model Definition: Creating Value (adapted from The Harvard Business School Definition)

Value Proposition	What value do you create for whom?
Income (Revenue) Drivers	How do you obtain money to create value?
Expense (Cost) Drivers	How do you spend money to create value?
Cash Flow	How do you maintain sufficient cash to sustainably create value?
Critical Success Factors	What are the key assumptions for sustainable value creation?

Sources of Data for Business Models: Financial Statements

- Annual Report
- Budget
- Profit and Loss (P&L)
- Cash Flow Statement
- Balance Sheet
- Financial Ratios?
 - Current Ratio
 - ROI (SROI)

Business Model: Value Proposition Defined

Value Propositions are brief descriptions of your organization and the value it provides, and articulate why the target beneficiary will choose your product or service offerings) over other alternatives. (Note: the alternative may be “non-consumption”).

Value Propositions often are sentences in the form of:

[Name of organization] provides [products/services], which are [statement of key differentiators], for [target beneficiaries], and thereby creates [statement of social value/impact], unlike [alternatives].

Aravind Eye Care System

Value Proposition Example:

For the millions of people in India with cataract blindness, the Aravind Eye Care System profitability provides diagnosis, treatment, and post-operative care, which is 100% safe, has a greater than 90% chance of cure, is less than 1/5 of the cost of comparable care, and is free for those who cannot afford to pay. Unlike government run hospitals, Aravind provides high-quality cataract surgery in a professional and ethical manner, serving all patients with dignity. Unlike those who do not receive quality surgery, patients are able to return to productive lives.

Value Proposition Example

Ideas at Work (IaW)

Ideas at Work - provides *a low cost, easy to use and maintain, manual water lifting device*, which is offered through a micro credit loan system to *rural Cambodians*, thereby building up credit history, while at the same time saving time and improving health—providing a solution that is superior to the three *available water pump alternatives in cost, ease of use, and maintenance*.



Value Proposition

Includes “Whole Product” Solution

- **Product:** laW provides a rope pump
- **Operations:** laW develops, manufactures, and distributes the rope pumps (value chain roles)
- **Service:** laW provides operation and repair training for the rope pumps
- **Market Creation:** Karaoke, product demonstrations, and customer testimonials educate the market and create sales
- **Financing:** laW arranges micro-credit for their rope pump customers

What are Elements of *YOUR* Value Proposition?

How Will You Capture Value to become Sustainable and Scale?

- **Product:** A physical item that creates value
- **Service:** Augmented product or information that creates value
- **Market Creation:** Activities that create awareness and educate the market
- **Operations:** Processes that create value
- **Financing:** Methods of enabling payment, creation of an *economic buyer*

Business Model: Income (Revenue) Drivers Defined

- Structures (Models)
 - Contributed
 - Earned
 - Hybrid (contributed and earned)
- Bases (Streams)
 - Occurrence-based (per time period)
 - Volume-based (per unit or per beneficiary)
 - License-based (per “use”)

Business Model: Income (Revenue) Drivers: Source of Income Budget

- Contributed
 - Source, Basis (Units, Amounts), Total
- Earned
 - Source, Basis (Units, Price), Total
- Hybrid
 - Contributed Income Business Unit(s)
 - Source, Basis (Units, Amounts), Total
 - Earned Income Business Unit(s)
 - Source, Basis (Units, Price), Total

Business Model Alternatives Classified by Key Income Drivers

CONTRIBUTED INCOME

- Grants
 - Income Drivers: Grants
 - Related Expense Drivers: grant writing, “grantor” management
 - GSBI Example: Med and Food for Kids (MFK)
- Donors
 - Income Drivers: donations (e.g., annual, per transaction)
 - Related Expense Drivers: fundraising, donor management
 - GSBI Example: Freeplay
- % of income from 3rd party
 - Income Drivers: Sales (%) of “corporate partner” products
 - Related Expense Drivers: partner management
 - GSBI Example: Pumpaid/WISH

Business Model Alternatives Classified by Key Income Drivers

EARNED INCOME

- Earned from Direct sales of products/services
 - Income Drivers: Sales volume and pricing
 - Related Expense Drivers: Sales/marketing, distribution, COGS
 - GSBI Example: Ziqitza (1298 Ambulance)
- Earned from third-party payments for products/services
 - Income Drivers: Sales volume and pricing
 - Related Expense Drivers: Marketing, COGS, 3rd party mgmt.
 - GSBI Example: Solar Suitcase
- Earned from Coop sales of products/services
 - Income Drivers: Sales volume and pricing
 - Related Expense Drivers: COOP Fees, COGS
 - GSBI Example: Aguada Guzman (Wool) Co-Op
- Earned from sales of student produced products/services
 - Income Drivers: Sales volume and pricing
 - Related Expense Drivers: Sales/marketing, training, COGS
 - GSBI Example: Fundacion Paraguayaa

Business Model Alternatives Classified by Key Income Drivers

EARNED INCOME

- Earned from licensing or franchising fees
 - Income Drivers: Number of licenses, license fee
 - Related Expense Drivers: Marketing, licensee management
 - GSBI Example: Sprinkles
- Earned from transaction fees
 - Income Drivers: Number of transactions, transaction fee
 - Related Expense Drivers: Transaction costs, partner mgmt.
 - GSBI Example: Thamel.com
- Earned from fees to join/subscribe
 - Income Drivers: Number of subscribers, subscriber fee
 - Related Expense Drivers: Marketing, subscriber management
 - GSBI Example: iEARN

HYBRID

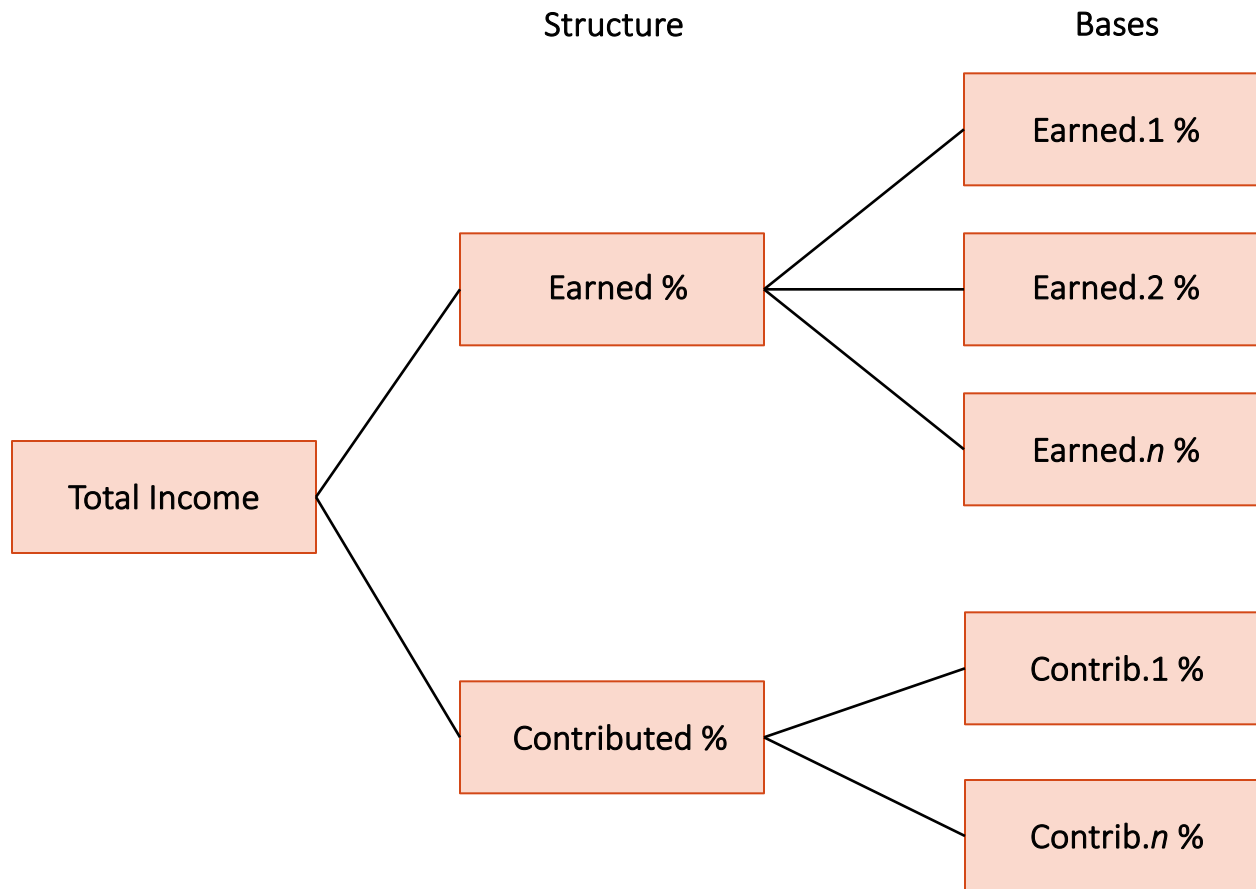
- Two (or more) organizations that share income and expenses with one (or more) with a contributed income model and one (or more) with earned income model
- GSBI Example: SAHAJ

Lessons from 167 Business Models

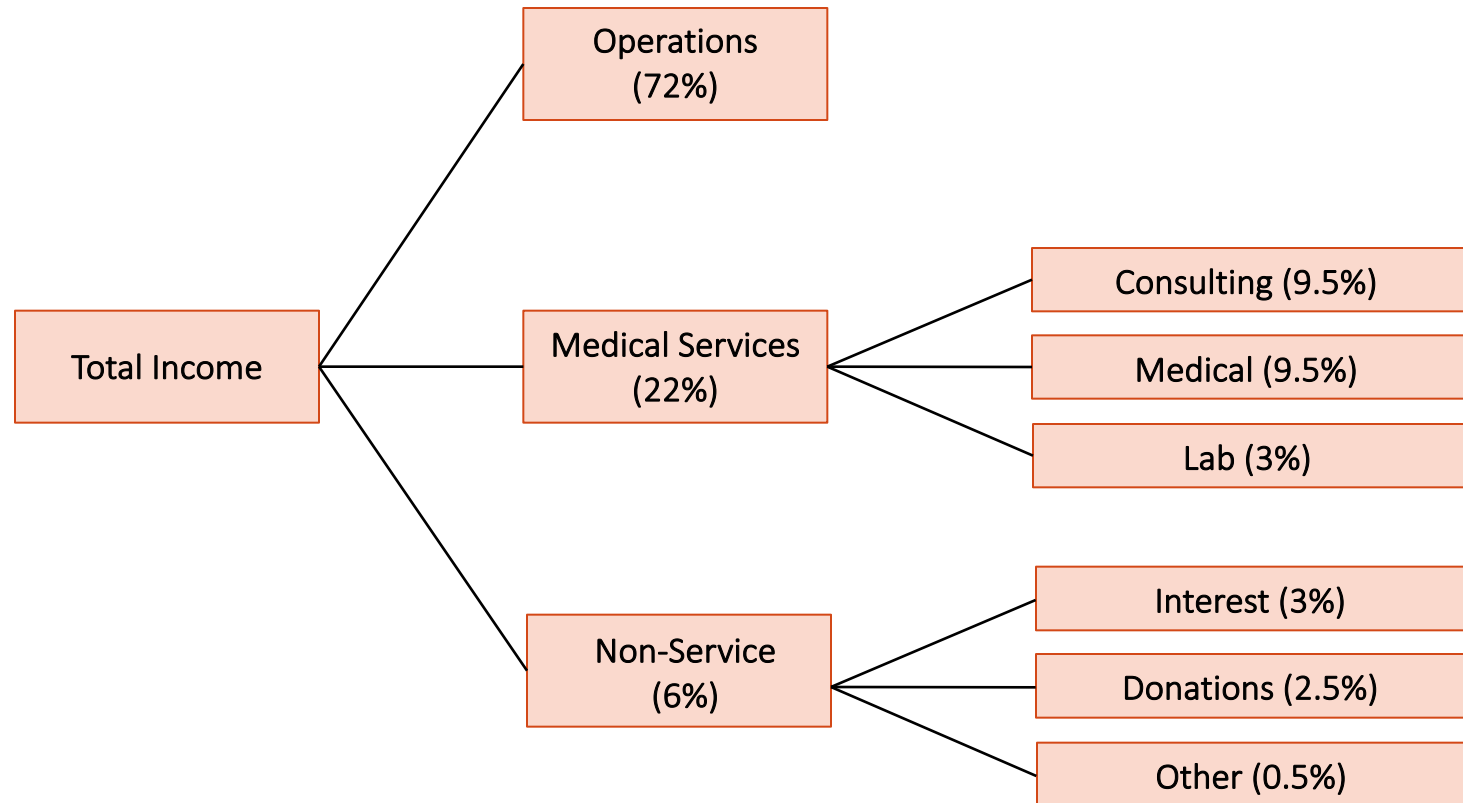
Possible Incremental Income Drivers

- “Cause” or “Project” related grants or donations
- “Cause related” marketing
- Additional (or related) product or services (e.g. support)
- Sell (product or service related) advertising
- Additional products or “pricing” to improve cash flow (e.g. micro-finance the “customer” or tiered pricing)
- License “intellectual property” (for other markets)
- Memberships/subscriptions

Business Model: Income “Fishbone Diagram”



Example: Aravind Eye Care System Income “Fishbone Diagram”



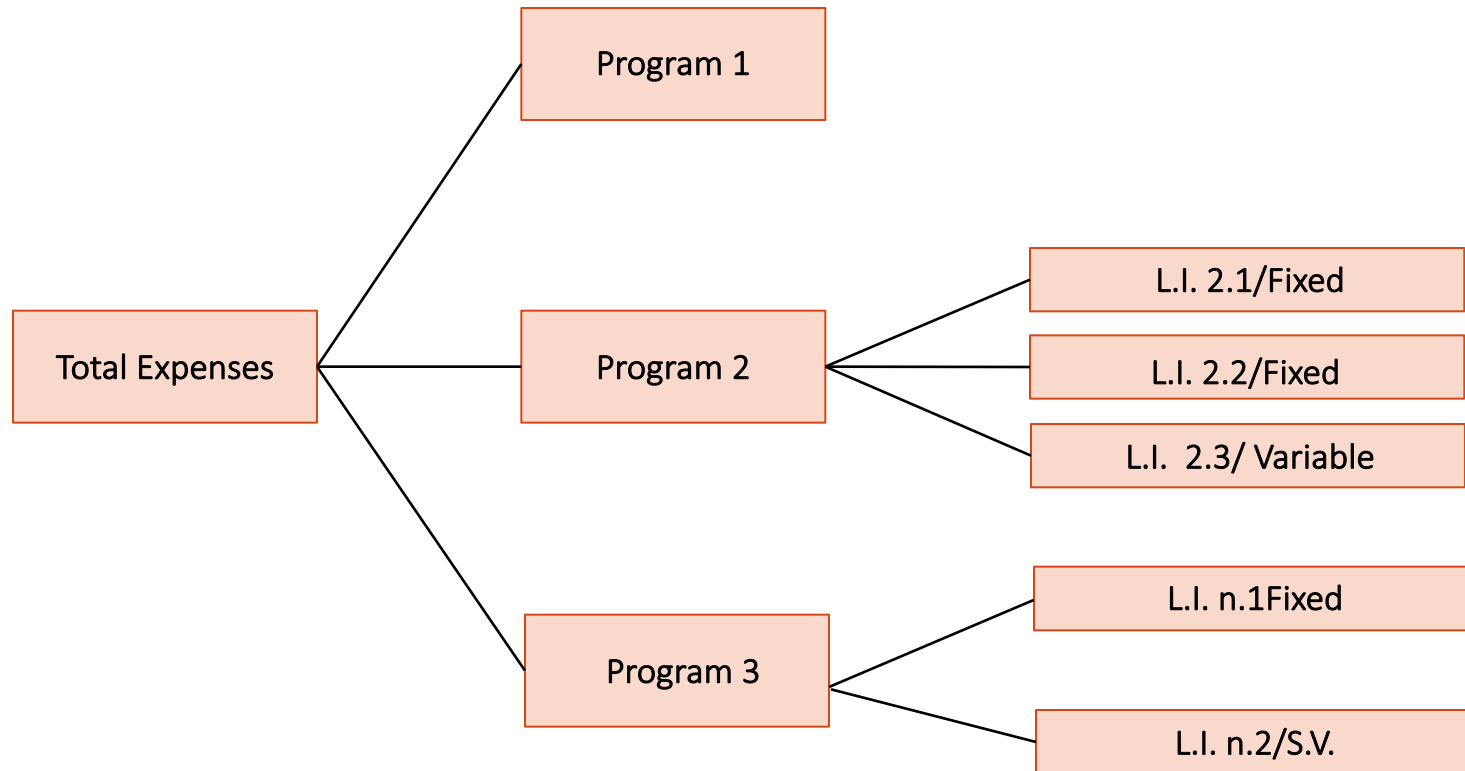
Business Model: Expense Drivers Defined: Line Item Budget

- Structures (Models) - at least one per major operation
 - Direct labor (payroll)
 - Indirect (support) labor (expenses for volunteers)
 - Materials/inventory/supplies
 - Marketing
 - Sales
 - Distribution
 - Facilities/equipment (Capital and/or depreciation)
 - Support/Customer Service
 - Administrative (including fund-raising)
- Bases (Streams)
 - Fixed
 - Variable
 - Semi-variable
 - Non-recurring

Business Model: Expense Drivers Defined-Ops/Program Budget

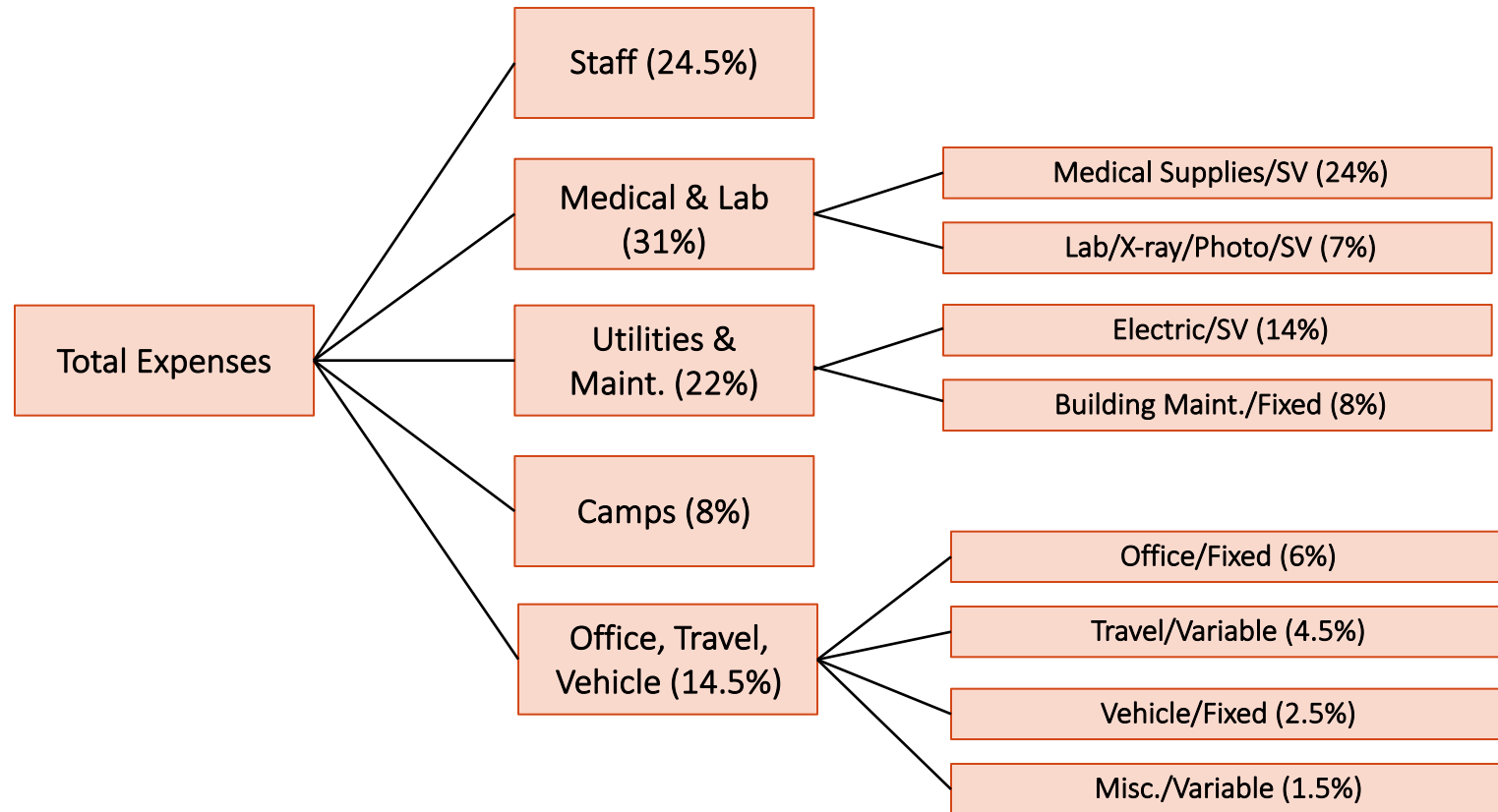
- Program: at least one per major operation
 - Line Item Expenses
- Bases (Streams)
 - Fixed
 - Variable
 - Semi-variable
 - Non-recurring

Business Model: Program Expenses “Fishbone Diagram”



Aravind Eye Care System Example

Line Item Expenses “Fishbone Diagram”



Lessons from 167 Business Models

Expense (Cost) Reduction Techniques

- Local (close to beneficiaries) labor and materials
- “De-skilling” (to use local, low-cost labor)
- Partnering (with local “experts”)
- Especially for manufacturing and/or distribution
- Dis-intermediation (eliminate the “middle-man”)
- M-commerce (use the cell-phone)

Business Model

Cash Requirements/Sources/Flow

- Initial financing
- Annual additional financing
- Cash flow statement (weekly/monthly/quarterly/annual)
 - Beginning cash
 - Cash inflows
 - Cash outflows
 - Ending cash
- Important cash dates
 - Maximum financing
 - Cash flow positive
 - Cash flow breakeven

Cash Requirements (Cash Flow Statement)

- Source: multi-year (quarter) budget
- Period by period statement of cash inflows and outflows (usually monthly or quarterly)

Year 1 Year 2 Period “n”

Cash Inflow

by source

- Cash Outflows

by use

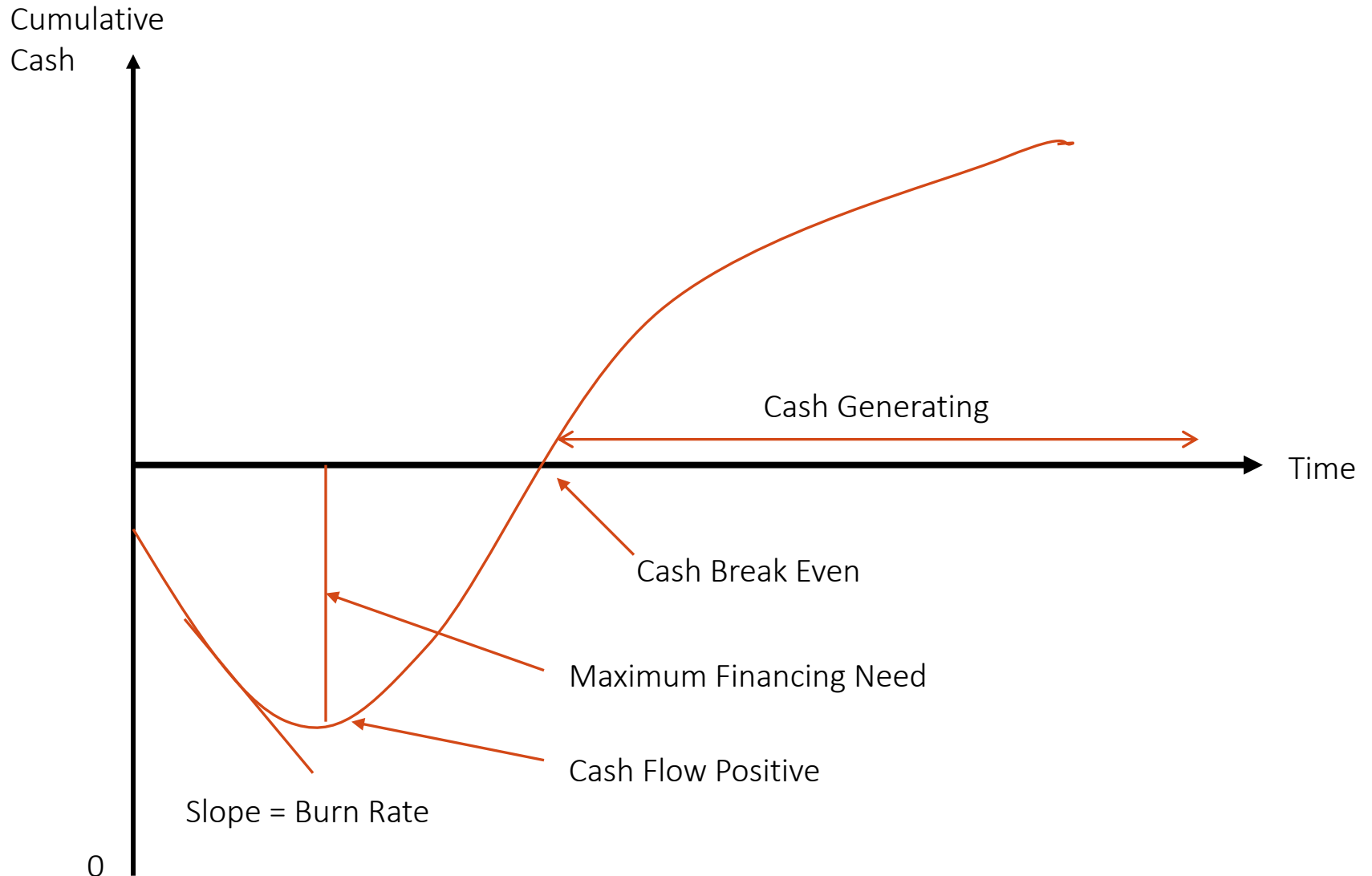
= Net Cash Flow

Beginning Cash

Ending Cash

Cash Balance

Cumulative Cash Flow Diagram



Ideas at Work

Cash Management Example (4 Years)

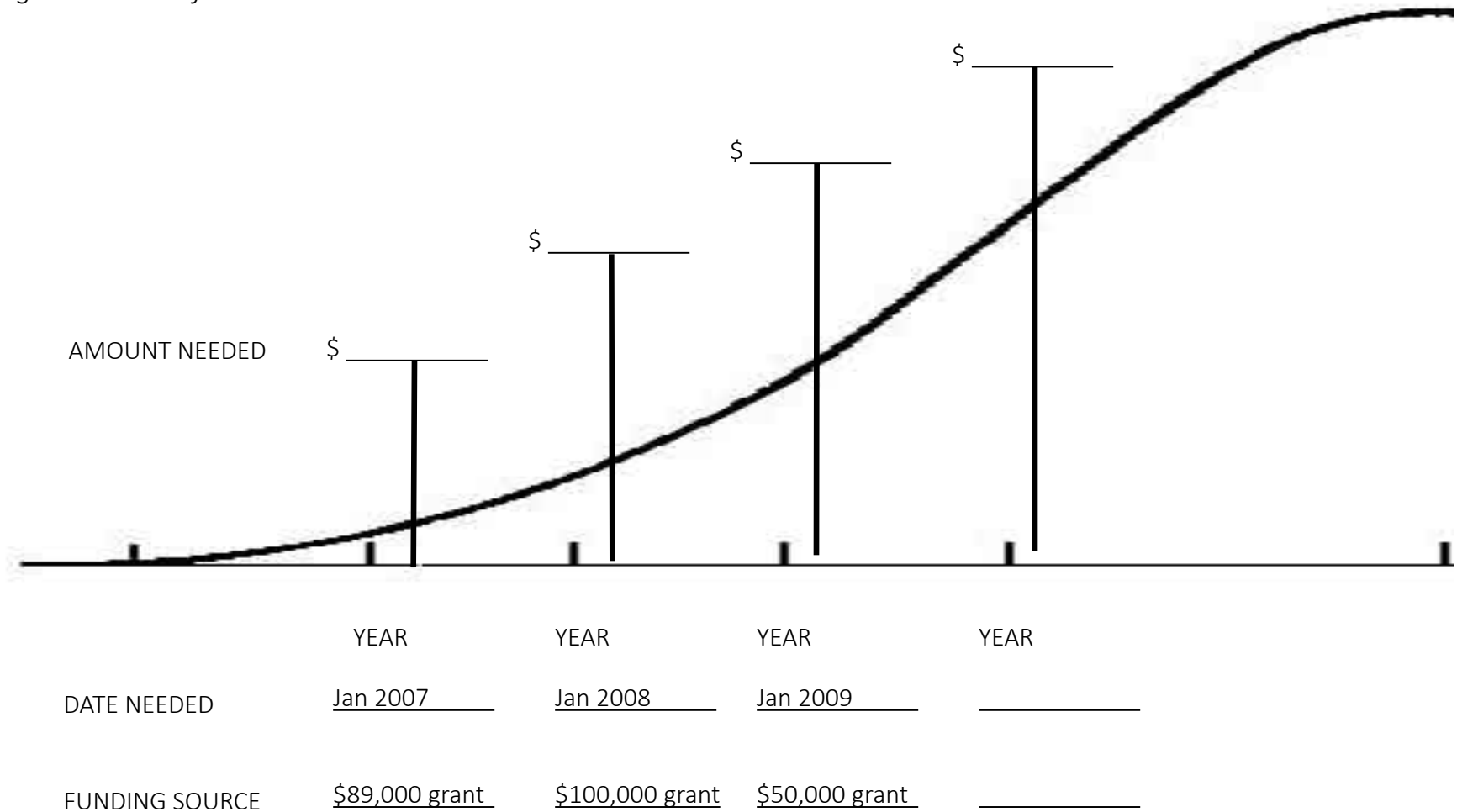
4 Year Cash Flow

	2007	2008	2009	2010
Starting Cash	\$ 40,000	\$ 37,553	\$ 25,408	\$ 17,938
Cash In	\$ 107,213	\$ 332,500	\$516,500	\$ 744,000
earned	\$ 19,000	\$ 232,500	\$466,500	\$ 744,000
contributed	\$ 88,213	\$ 100,000	\$ 50,000	
Cash out	\$ 109,660	\$ 344,645	\$523,970	\$ 655,895
operation	\$ 60,700	\$ 206,045	\$278,270	\$ 307,895
cost of goods	\$ 48,960	\$ 138,600	\$245,700	\$ 348,000
Ending Cash	\$ 37,553	\$25,408	\$17,938	\$106,043

Ideas at Work

FINANCING PLAN

What is the timing (date) and amount of funding needed and from what source?



Business Model

Critical Success Factors (CSF) Defined

- Key assumptions (risks/opportunities) regarding income, expenses, and cash flow
- Income
 - Funding environment
 - Funding sources
 - In-kind donations
 - “Market” for products/services
 - Quality of products/services
- Expense
 - Beneficiary environment (interest)
 - Partnerships
 - Manufacturing (capability/quality)
 - Infrastructure

Aravind Eye Care System: Critical Success Factors

- Low-cost workflow for eye care system
- Successful training of all staff
- Maintain > 40% paying clients
- Re-invested surplus in staff training, improved processes, and new technology
- Motivate staff through work environment and competitive compensation
- Use partnerships for in-field diagnosis and for new technology development

Unit Economics (for a firm)

- Definition: Method used to determine whether a business model can be successful [profitable] by calculating if an individual unit of the good or service would be profitable. For example, if Mountain Mike is considering opening a store which sells pizza, he would calculate the cost of making one individual pizza, and compare it to the price he would charge for the pizza. If the profit is positive, the business is thought to be profitable.
- Method: Take your primary income model and lay out the revenue and cost drivers for a single unit in your business [e.g., product, customer, store].

Unit Economics (for a Supply Chain)

- Definition: The income (and expenses) for each organization in the supply chain receives for a unit of product or service that is delivered to a customer by that supply chain– determining whether or not each organization in the supply chain is profitable on a per unit basis.
- Method: Take the final amount (retail price) received for the final product or service and determine how it is “allocated/shared” among the firms in the supply chain (all the way to base suppliers) according to the amount each firm (“unit”) in the supply chain will receive. Determine if the amount for each “unit” in the supply chain is sufficient for it to be able (financially) to perform reliably.

Supply Chain Unit Economics Example: For **one** chocolate bar

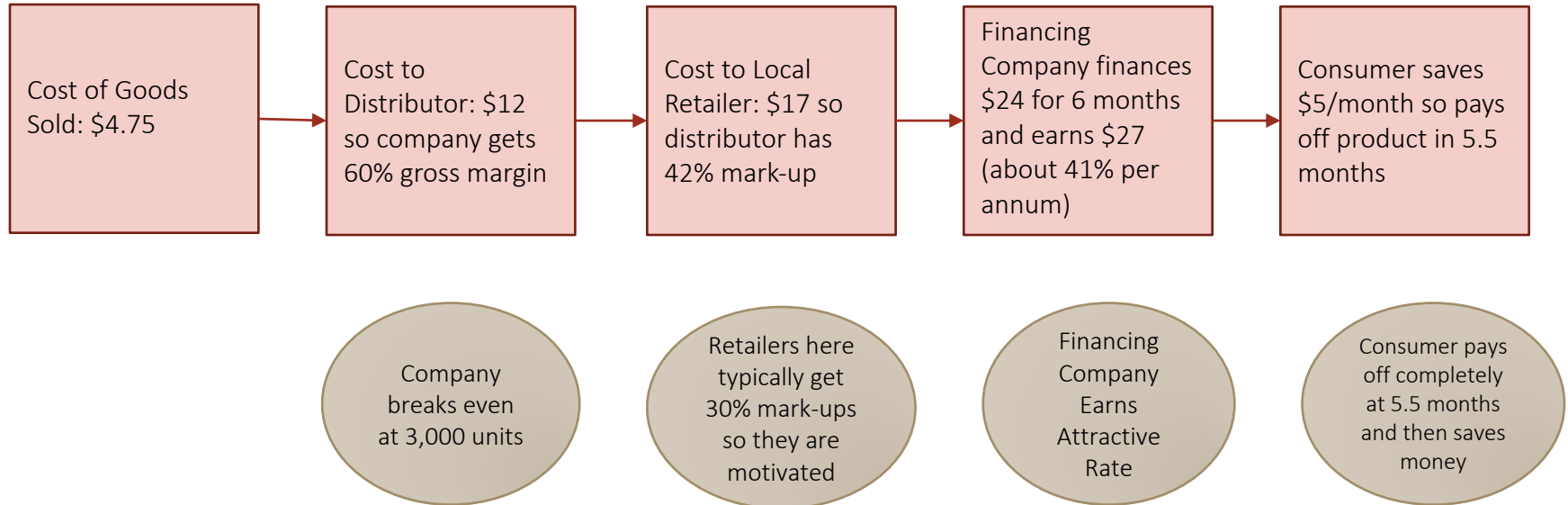
	Unit Revenue	Unit Cost	GM Unit	GM%	Fixed Cost	Break-Even Units
Farmer	.50	.25	.25	50%	\$300	1,200
COOP	.75	.60	.15	20%	\$1500	10,000
Processor	1.20	.90	.30	25%	\$12,000	40,000
Factory	2.00	1.60	.40	20%	\$25,000	62,500
Distributor	3.10	2.60	.50	16%	\$200,000	400,000
Retailer	3.99	3.20	.79	20%	\$500	633

Unit Economics Along the Value Chain: Solar Lantern Example

Solar Lantern Product	Costs/Prices	-	
Lantern Assembly	\$ 2.30		
Solar Battery	\$ 1.50		
Assy & QA	\$ 0.95		
Total Unit COGS	\$ 4.75	40%	COGS
Price to Distributor	\$ 12.00	60%	Gross Margin for Company
Price to Local Retailer	\$ 17.00	42%	Distributor Mark-up
Product Price to Consumer	\$ 24.00	41%	Local Retailer Mark-up
Financing Cost to Consumer	\$ 3.00		
Total Price to Consumer	\$ 27.00		Customer saves \$5/month in kerosene so pays back full price in 5.5 months

Unit Economics Along the Value Chain: Small Lantern Example

Discussion (Your Organization)



Unit Economics for Social Businesses “Issues”

- Units
 - How to choose?
 - What about multi-part units (e.g. product and service)
 - What about multiple types of units (multiple products or services)?
- Income per unit
 - What if all income is contributed?
 - What if each unit is subsidized (or free)?
 - What if one type of unit subsidizes another?
- Expenses per unit
 - Allocated over multi-part units?
 - Allocated over multiple types of units?
 - What about capital expenses?

Business Model: Unit Economics Example

Aravind Eye Care System

1. Unit = cataract surgery

2. Average income, expenses, surplus per unit
(FY 2002, source: Prahalad): 196,425 units
(68,055 paid)

Income*	388M R	=	1,975R per unit
Expenses**	177.5M R	=	904R per unit
Surplus per unit		=	1,071R per unit

* for all paid units

** for all units (paid or free)

The Financial Plan (an Appendix to the Business Plan)

- Business Model (5 Parts)
- Financing Method and Requirements
- Budget (3 year)
- Financial Metrics (e.g. Unit Economics)

Report #6: Business Model

NOTE: THESE ARE NOT THE SAME AS IN CARLSON/KOCH

1. What is the Value Proposition? What are the key differentiators from the alternatives?
2. What are the key income drivers? Give one suggestion for additional (or fewer) income drivers to improve sustainability and scalability.
3. What are the key expense drivers? Give one suggestion for major expense reductions that does not decrease impact or income.
4. Does the cash flow (or income or budget) statement support financial sustainability (positive cash flow) and scalability ($\% \text{ income growth} > \% \text{ expense growth}$)?
5. Given the Value Proposition, what is the “best” unit for unit economics. If possible, using this unit, compute the unit economics for your organization for the first (or total over all) year(s) of the financials.

Discussion of: Business Model

1. What is the Value Proposition? What are the key differentiators from the alternatives?
2. What are the key income drivers? What are the key expense drivers?
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