Billion Dollar Company: An entrepreneur's guide to business models for high growth companies©

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Preface

This book is devoted in part to a systematic approach to developing a business concept and to a greater degree to a formal process for creating a business model. To put these two themes in context, I first need to explain my view of a business and, in particular, how to build a large business. Business is a conflict between revenue growth and cash flow. In a properly managed business, one is always trading off revenue growth objectives and cash flow availability.

The constant effort to grow the business has many benefits, some of which are listed below:

- Growth tends to force one to constantly follow the customer and their changing needs and expectations
- Growth tends to produce economies of scale and lower unit costs
- Growth tends to force constant improvement in all areas of the business in terms of policies, procedures, operations and customer service (what the Japanese call *Kaizen*)

- Growth tends to be attractive to both early stage and public company investors, which may provide the capital to continue growth

All of these benefits, of course, cannot be achieved if the business runs out of cash. If the business runs out of cash, the business is dead. Therefore, any growth strategy has to be measured against the risk of running out of cash in the short term or before more cash can be raised. Cash flow, of course, is also the ultimate determinant of value in a business, which again creates a conflict with growth.

While profitability is obviously an objective, as long as the business has cash one really only needs to manage to achieve a future positive cash flow (or worse case a breakeven cash flow) before cash runs out. In other words, profitability is the third objective.

A startup company's objectives in order of priority are:

1. ***Revenue growth***
2. ***Positive cash flow***
3. ***Profitability***

It is comparatively easy to manage margins to achieve profitability and much harder to attract customers and turn them into revenue.

The first three stages in the life of a business are shown below.

Stage	Revenue
1. Proof of Concept	0-$1 million
2. Commercialization	$1-3 million
3. Scaling the Business	$3-10 million

Proof of concept is the stage where you have a marketable product and one is madly running around looking for anybody who will buy the product. Commercialization is where you have identified a customer segment on which to focus but you still lack the proof that this segment has potential. Scaling the business is when you demonstrate that a large customer base can be served typically with positive cash flow results or even profitability.

Many businesses get stuck at revenue of less than $5 million, as the statistics in the Foreword showed, because they cannot manage the tradeoffs between revenue growth and cash flow or they prematurely focus on profitability. After demonstrating that a customer base exists in Stage 2, all effort should be focused on scaling the business (Stage 3), which is in large part executing on a growth strategy.

While I hope that my discussion of business concept and business model has some value to the reader, an equally important objective is to develop in the reader an attitude or a discipline in developing a business model using my formal methodology. The formal methodology is quantitative, but not advanced mathematics, and much of the discipline comes from reducing the thinking on business model to numbers. To paraphrase the quote from Lord Kelvin at the beginning of the book--if you cannot explain it in numbers, your knowledge is unsatisfactory. The elegance and simplicity of numbers also greatly facilitate understanding of the business model by investors. In fact, many sophisticated investors now read the financial model before the business plan because it is an easier way to understand the business model. A significant part of the discussion focuses on building self-explanatory models. Decision makers review this type of model (and do not need to delegate analysis to junior staff).

The discipline of reducing the business model to numbers has two other benefits, which are discussed in Chapter 4.

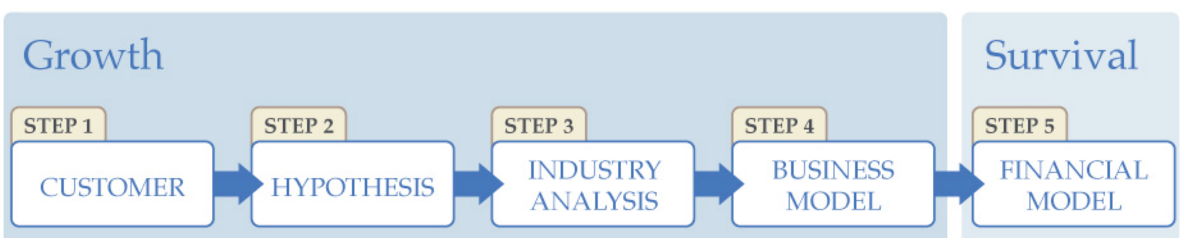
1. ***The risks in the business model are easy to identify***
2. ***The key performance indicators (KPI) for managing the business are identified***

The development of a business concept is perhaps the most misunderstood and challenging part of a startup. Inadequate course material at many universities is partly to blame. Web-based templates for a business plan also come in for part of the blame. Lastly, most people only develop one business concept in their lifetime and rarely take the time to write about the process. Simply put, a business concept must address four questions:

1. ***What is the customer need?***
2. ***What is the value proposition?***
3. ***What is the differential or competitive advantage?***
4. ***What is the size of the market opportunity?***

What separates my methodology for developing a business concept from most others is the heavy reliance on formally developing the business model (Step 4) and how it links to the financial model, which is what most of the remainder of this book is about. I teach a five-step process to develop a business concept, which also makes it easy to write a business plan, produce a financial model or prepare a PowerPoint for an investor.

The five steps are shown below.



The first three chapters of the book briefly deal with customer, hypothesis and industry analysis. I discuss them to set the stage for the discussion of business model and financial model, which are discussed in the next nine chapters. I conclude the book with a chapter on how to use the business model to manage the startup and the cash flow of the business.

Each chapter in the book concludes with real examples from Indonesia that illustrate the major theme of the chapter. One benefit from building a $1 billion company in seven years is the abundance of examples to illustrate concepts.

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