The Overemphasis on Business Plans in Entrepreneurship Education: Why does it persist?

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Abstract

A quintessential aspect of entrepreneurship academic programs is a course on business plans. However, in reality business plans are enigmatic. Business plans are said to be critically useful for entrepreneurs but most entrepreneurs don’t prepare them. Business plans are supposed to lead to entrepreneurial success. However, the correlation between start-up business plans and business survival has been found to be weak. Business plans are said to be a requirement for business start-up financing. However, financial institutions, especially banks, have more objective criteria of determining credit worthiness than relying on written business plans. In view of these doubts about the “functionalities” of business plans, there is a growing voice to de-emphasize them in entrepreneurship education programs. George Gendron, former editor of Inc magazine for 20 years, and David Gumpert, who had already written several textbooks on business plans and is a practicing entrepreneur, have urged educators and entrepreneurs to “forget” business plans. Amar Bhide, of Harvard Business School, among other well-known academic institutions, has attempted to explain why a de-emphasis of the business plan in entrepreneurship education programs is very unlikely in the foreseeable future. The paper evaluates the doubts on the functionalities of business plans and the reasons why de-emphasizing them is unlikely. The paper also contains some recommendations for pedagogical changes to make business plans meet the needs of students more than they do now.

Keywords: Business plans, entrepreneurship, business start-ups, entrepreneurship education

1. Introduction

A quintessential aspect of entrepreneurship academic programs is a course on business plans (Perry 2001, Fregetto 2005, Bhide 1999, Hallam, 2014, Simon 2015). The reason for this is the wide-spread thinking that a business plan is a necessity for every entrepreneur (U.S. SBA 2015, Zahorsky 2015, Siropolis 1997). However, in reality business plans are enigmatic. Business plans are supposed to be critically useful for entrepreneurs but most entrepreneurs don’t prepare them (Siropolis 1997, Holtz 1994, Hallam 2014). Business plans are commonly assumed to lead to entrepreneurial success. However, the correlation between start-up business plans and business survival has been found to be weak (Perry 2001, Sahlman 1997, Lange, 2005). Business plans are said to be a requirement for business start-up financing. However, financial institutions, especially banks, have more objective criteria of determining credit worthiness than relying on business plans. Venture capitalists often require business plans, but they finance less than 1 percent of business start-ups (Bhide, 1999). Leading voices on entrepreneurship education have called for a de-emphasis on business plans, asking academics and business advisors to “Burn the business” (Gumpert 2003), or to “forget the business plan” (Gendron 2007), or to “influence the conversation so that entrepreneurship is not all about writing a business plan” (Simon 2015). However, most entrepreneurship educational programs in the U.S. and abroad continue to emphasize the business plan (Hallam, 2014). This paper examines the gap between the theoretical and practical aspects of business plans and why that gap, the overemphasis on business plans, persists.

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2. The Entrepreneurial Mindset and Entrepreneurial Intentions

“If business plans are so important why do so few people actually write them?” This is said to be the second leading frequently-asked question about business plans. The first leading question is “Why do I need a business plan?” (Zahorsky, 2015). There is no shortage of answers to this question, as we have seen in the introduction. However, the question of why so few people write business plans, remains a puzzle. Some have attempted to answer it by referring to human frailties such as procrastination or overconfidence or even a tendency to not wanting to know one’s weaknesses (Zahorsky, 2015). In reality, the number of entrepreneurs who prepare business plans has been found to be as low as 5% at start-up stage (Sexton and Van Auken, 1985, Holtz 1994, Karger 1996, Siropolis 1997, Rue and Ibrahim 1998, Mazzarol 2001, Donkels and Dupont 1987, Lange et al, 2011). And the few entrepreneurs who prepare business plans barely use them (Zimmerer & Scarborough, 1995). Why business plans are not prepared by entrepreneurs has become a popular topic for academic research. Amar Bhide (1999, 2003) offered three reasons why most start-up entrepreneurs, even those who are highly successful, such as Bill Gates, don’t prepare written business plans. These reasons are: very successful businesses are started in highly turbulent environments making meaningful planning impossible, many entrepreneurial opportunities are very time-sensitive and disappear too fast to allow comprehensive planning, and most business start-ups don’t require much capital so that business failure isn’t financially painful. Allan Gibb (1999) explains that typical entrepreneurs don’t prepare business plans because such behavior is inconsistent with the entrepreneurial mindset or way of life. According to Gibb, the entrepreneurial way of life is epitomized by; among other things, the disposition for great freedom in making decisions about business and the relationship between business and social/family life, and reliance on informal alliances to manage interdependence with different stakeholders. Bangs (1992) refers to “the man of action problem” commonly associated with entrepreneurs. Entrepreneurs have a preference for doing things instead of thinking about them, let alone writing about them. Wally (Famous) Amos (1999) earned himself a name for telling entrepreneurs to “Just Do It” instead of preparing formal business plans. The overwhelming number of entrepreneurs are contented with what Mazzarol (2001) has called “intuitive planning” or what Van Auken and Neeley (2000) have called “undocumented pre-launch preparations”. Start-up entrepreneurs, especially those with business experience, skip business plans and rely almost exclusively upon their intuition that has been sharpened by experience (Dane & Pratt, 2007; Gendron 2007) Further, a large number of entrepreneurs are “micro-entrepreneurs”. They focus on “lives outside the business and the freedom that the business bestows” (Carland and Carland 2003). In general, these entrepreneurs don’t devote time to planning.

3. Business Plans and Entrepreneurial Success and Failure

There is a popular assumption that business plans lead to entrepreneurial success. William Sahlman commented “...judging by the hoopla surrounding business plans, you would think that the only thing standing between a would-be entrepreneur and spectacular success are the [elaborate business plans] (1997).” He added that in “his experience with hundreds of entrepreneurial start-ups” business plans rank near the bottom as a predictor of new venture success, and that the more elaborately crafted the business plan is the more likely the venture is to fail. Research on whether business plans make any difference on entrepreneurial success or failure has generated conflicting conclusions. First, most studies that have attempted to discover a relationship between business plans and entrepreneurial success have not focused on start-up entrepreneurs. The focus of most of these studies has been on business planning to continue and/or to grow the business. This is strategic planning. Strategic planning and business or entrepreneurial success have often been found to be positively correlated (Karger 1996, Mazzarol, 2001, Carland and Carland, 2003, Kaplan & Bienhocker 2003). Two studies that are known to have focused on written start-up business plans and start-up business success found that business plans made marginal or no difference in business success or failure. In one study (Perry 2001) it was found that entrepreneurs who started out with and without business plans succeeded or failed to nearly identical degrees. In another study, appropriately titled “Do Business Plans Make No Difference in the Real World?”, researchers at Babson College (Lange et al 2005) discovered no difference in the performance of businesses started with and without business plans. It has also been found that business planning increases with business size. Most business start-ups are very small in size and largely don’t prepare business plans. However, some of the start-ups which survive, a measure of business success, do eventually undertake business planning (Bewayo, 2010). They plan in order to attract funding for business growth. Also, they plan to better deal with external stakeholders, such as suppliers and distributors (Gibson & Casser, 2002). It appears that business success leads to business planning, a phenomena which has been described as “practice precedes planning” (Mazzarol 2001). That is, business planning doesn’t lead to entrepreneurial success. Rather, entrepreneurial success leads to business planning.
4. The Business Plan as a Financing Tool

Acquiring business financing has been cited as the major or most important reason for writing business plans (Kaplan and Warren 2013; Ford, Bornstein & Pruitt 2007). However, current evidence fails to clearly show that financial institutions, especially banks, require business plans in order to grant start-up business loans. The widely-quoted 5 Cs that business lenders use to evaluate loan applications do not include business plans. So, a bank will grant a business loan if the applicant has good credit worthiness (character), the applicant can show that the business will generate enough income to pay off the loan (capacity), the applicant has enough money to put down as “down payment” (capital), the applicant has assets to pledge for securing the loan (collateral) and the applicant’s proposed business is in an industry that isn’t known to be too risky (conditions). Some research has shown that banks frequently grant loans without requiring business plans (Van Auken & Horton 1994) and that business plans are required only as a last resort. It is also known that when banks require business plans, they want to see “summary” business plans, not the comprehensive business plans that are popular in business plan courses (Hatten 2013). Summary business plans average about 6 pages and contain the specific information a given bank needs in order to evaluate loan applications. Bank loan officers have been known to help the loan applicant fill out the summary business plans, often in the form of a “loan proposal” (Kaplan & Warren 2013). In general, venture capitalists require business plans before making investment decisions. According to Amar Bhide, entrepreneurs are of two main categories: those who plan a venture very carefully and everyone else. Those who plan their ventures very carefully have gotten most of the media attention because they tend to be associated with venture capital (Bhide 1992, Bhide & Bartlett 2003). It appears that they also get most of the attention from the academic community. However, entrepreneurs who plan are commonly known to be no more than ten percent of all start-up entrepreneurs (Holtz 1994, Mazzarol 2001).

According to David Gumpert, and relying on his own business experience as well the experience of many other entrepreneurs, only a small fraction of start-up entrepreneurs with business plans get funding from venture capitalists. Gumpert gained great fame for his now-famous “Burn your business plan, what investors really want from entrepreneurs” treatise, published in 2003. Gumpert, as well as Allen (2012) argued that venture capitalists very rarely fund business start-ups before such start-ups show solid evidence of success. Venture capital, similar to bank loans, tend to shy away from early stage or start-up financing. Gumpert pointed out that “carefully crafted business plans are rejected out of hand by venture capitalists” (2003). Interestingly, Gumpert had earlier authored two major works on business plans: “Business plans that win $$$”, published in 1987 and “How to really create successful business plans”, published in 1998. Earlier, we stated that there is a tendency for entrepreneurs to prepare business plans after seeing signs of success in their start-up enterprises. The business plans written in these instances are for growing businesses, not launching them. The business plans taught in business plan courses or “new ventures” courses are mostly for business start-ups. However, start-up entrepreneurs rarely prepare business plans. Sahlman(1997) argued that the reason why many business plans don’t attract investor financing is because they contain too much “ink on numbers”. He claimed that a great deal of financial projections in business plans are imaginations because entrepreneurial ventures face too many “unknowns” to predict revenues and profits. Sahlman points out that the average venture capitalist is going to discard these projections in most cases. Students are made to spend most of their time formulating these financial projections in business plan projects or courses. The financial section is also the hardest part of the business plan to teach (Moyes, Azriel and Schenkel 2007). However, if most of the financial projections are discarded by venture capitalists because they are imaginations, should they be prepared? Researchers at Babson College stated that there was no “compelling reason to write a detailed business plan” unless the prospective entrepreneur will be seeking substantial amounts of capital (Lange et al 2005).

5. Problems with the Business Plan Pedagogy

Even if students learn how to prepare business plans, they do not use them to start their businesses reasonably soon after graduation. R. Peterson, K. Westmoreland, M. Liston, and A. Deshmukh point out that “Most entrepreneurial programs gear students toward starting their own enterprises, yet... most students will not do so until their 30s to 40s” (2009). It is very likely that the skills gained in the business plan course will not be retained and put to use (Watson 1963, Lange 2011). This is especially the case with undergraduates. They prepare business plans that literally go to waste.
A suggestion has been made that these business plans be made available to would-be entrepreneurs in the community (Achua & Lussier, 2005) It has become standard practice to use the student team approach when teaching business plans. For large classes, this is almost a practical necessity (Fregetto 2005). It is also a great opportunity for students to develop team building skills. Moreover, by dividing the sections of the business plan between team members, students can prepare a complete business plan in one semester, which is often a problem (Bell & Herring 2007). However, the student team approach doesn’t let the individual student pursue his/ her own personal interest in terms of business opportunities. The business plan project in a course is approached as a mere class exercise, not a tool for predicting business and personal success. Much of the information used, such as owners’ equity investment and business/industry skills, is often imagined. It is, therefore, not surprising that the business plans prepared for meeting course requirements are rarely turned into “live” businesses (Hallam, 2014). Business plan writing has become a growth industry. On the Internet, a student can access any number of “ready-made” business plans and business plan section templates. As a result, business plan plagiarism has reached high proportions (Lahm & Stowe 2008). Admittedly, academic plagiarism is not unique to business plans; students have been doing it for many decades throughout all academic disciplines (McCabe 2001). However, the fairly standardized structure of business plans (Gumpert 1997) and the huge amount of ready-made business plans on the Internet make business plan cheating relatively easy. It is reported that 75 percent of college students have admitted to academic cheating (McCabe 2001). Therefore, the only reason why a student will invest the time to conduct market research for preparing his/ her course business plan, is the knowledge that a fake or mimicked business plan will not help his/ her business, when one is started. We have just pointed out that student-written business plans, especially at the undergraduate level, are not commonly used to start actual businesses. Most students have no personal and compelling reason to prepare really good and “honest” business plans. It should be stated that these pedagogical problems that surround business plans are not as pronounced at the graduate level as they are at the undergraduate level. An explanation for this is that graduate students are more likely to use course-required business plans to embark on business start-ups. This is because they are nearing their 30s and often have some work experience, factors that are favorable to starting businesses (Lussier & Corman 1995, Hallam et al 2014).

6. The Business Plan as a Crutch and Some Recommendations

An admiring interviewer from Inc. magazine asked entrepreneurship guru Amar Bhide the following question: “Given your findings, why is there so much emphasis on business plan writing in entrepreneurship programs?” (Bhide & Bartlett, 2003) According to Bhide, because researchers, academic or others, “haven’t collected much systematic knowledge about starting new businesses, instruction on how to write a business plan becomes a crutch” (Bhide & Bartlett 2003). He added that given the growing demand for entrepreneurship education, academic institutions have had to create new courses. Business plan courses “are easy to generate”. Instructors in entrepreneurship programs teach business plans because alternative educational materials are lacking. One can also speculate that teaching business plans, especially given all the teaching tools available, is easy to master. It is easier to master than mastering teaching softer aspects of entrepreneurship such as risk-taking, creativity or dedication. An old debate about entrepreneurship relates to whether entrepreneurship is more about personality traits than it is about entrepreneurial objective behaviors (Gartner 1988; Carland, Hoy & Carland 1988).

The business plan neatly summarizes what entrepreneurs do: they conduct market research, they project sales, raise capital, assemble management teams etc... The choice to place the emphasis on business plans seems to imply that entrepreneurial success is assumed to be more about what entrepreneurs do than who entrepreneurs are. It is also easier to discuss what entrepreneurs do than how risk-taking they are or need to be.Bhide suggests that it is time to reduce the emphasis on business plans and dwell more on subtle entrepreneurial personality qualities such as “opportunistic adaptation” (Bhide & Bartlett, 2003). George Gendron, formally the chief editor of Inc. magazine for two decades, has taken a more radical approach. Founder and former director of the Entrepreneurship and Innovation program at Clark University, he tells would-be entrepreneurs and academics to “Forget the elaborate business plans” (Gendron 2007). At Clark (http://www.clarku.edu/clarkinnovation) there is no business plan course. Gendron argues that business plans are used for attracting venture capital. But less than 1 percent of business start-ups are funded by venture capital. Also, the program is open to every academic major, not just business majors. Additionally, they have several entrepreneurs-in-residence, who not only teach most of the courses in their program, but also are mentors to each student in the program. Probably most academic programs in the U.S. cannot go the Clark University way. However, especially at the undergraduate level, entrepreneurship programs should consider requiring students to conduct market research and prepare only feasibility analysis or opportunity analysis.
Many authors of textbooks on entrepreneurship recommend that full business plans should be prepared only after conducting feasibility analysis. Entrepreneurship programs at the University of Colorado, Florida State University and the University of Southern California have courses that focus exclusively on feasibility analysis or studies (USABSE 2010, University of Colorado 2009). Feasibility analysis normally doesn’t get into marketing strategies and covers no more than 10 pages. Because it is relatively restricted in coverage, students can prepare meaningful feasibility analyses in one semester. It can also be done on an individual basis. These factors would help mitigate some of the pedagogical problems surrounding business plans to which we alluded earlier. Further, feasibility analysis would leave some time to consider subtle behavioral traits that go with successfully starting and managing a business. The over-emphasis on business plans in most entrepreneurship education programs commonly results in stand-alone business plan courses, where comprehensive business plans are written by students. The need for such business plans has been questioned (Lange 2005, Sahlman 1997, Bhide, 1999).

Eliminating full business plans from entrepreneurship programs is unlikely in the foreseeable future. First, most students who write business plans use them for launching their businesses when they do so immediately after graduation (Lange et al, 2011). Such business plans are prepared with a specific business idea in mind. They are not prepared as mere academic exercises, which is typically the case in most business plan or new ventures courses (Achua, C. & Lussier 2005, Hallam et al 2014). At the University of Texas at San Antonio an effort is made to get students write business plans related to identified real business opportunities (Hallam et all 2014). Students who, for whatever reason, possess deep entrepreneurial intentions, will very likely use their written business plans to launch business ventures. It has been frequently argued that entrepreneurial behavior is planned behavior (Fayolle and Gailly, 2015, Hallam, 2014). Business plans assist in the process of turning planned/intended behavior into actual behavior, because they increase a prospective entrepreneur's self-efficacy. A pedagogical implication of this is that writing business plans is better suited for students already strongly inclined toward the entrepreneurial path. This means that only students who “elect” to take business plan courses stand to benefit most from such courses. Business plan courses should be elective courses in entrepreneurship academic programs. However, it is reported that the business plan is considered to be the most important feature of the top 100 entrepreneurial academic programs in the country (Hallam, 2014). Accordingly, the business plan course is predominantly a required course. Business plans often positively influence students toward entrepreneurial careers. Students who write business plans are said to be twice as likely to launch business ventures as students who don’t write business plans (Gartner 1988, Henricks 2008, Lange 2011). However, the influence of business plans on students was found to be not as strong as that of taking other entrepreneurship courses (Lange et all 2011). Lange et al (2011) recommended that “educators should not stop teaching how to write business plans, but they should not overemphasize it”.

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