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Moonpig.com – Do MBA Business Plans Really Work? Part 1: Against All the Odds

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Abstract. The case study is the first part of a three part case study series that tells the story of Moonpig.com, a UK innovative high-growth company that started in 1999 when Nick Jenkins progressed from writing his first MBA business plan to create one of today's most successful Internet-based greeting card businesses. The case series vividly demonstrates how an overly optimistic and detailed MBA business plan, even with frequent reiterations and modifications, was nonetheless key to the development and financing of a finally successful company. There are lessons, however, for teachers and students alike in the preparations of such plans and the management of the process for attracting what Nick Jenkins termed investors' 'hope money'! Part 1 describes the first three years of Moonpig.com. Following several reiterations of the original business plan, which required a £50,000 investment for a business predicted to be profitable in 12 months, the business was forced to raise £2 million of new investment while still predicting profitability within 12 months' time. Part 1 focuses on whether to invest a further £300,000 into the business in 2002 and if yes, under what conditions. It also raises the question on how to grow the business further. A detailed Teaching Note with an analysis and suggestions for questions is also available to stimulate discussion in the classroom. (Moonpig.com Part 2 and 3 are also published in this edition of the International Review of Entrepreneurship).

Keywords: entrepreneurship, business plans, Dot.com companies, greeting cards/ publishing, business angels, venture capital, company valuation, business growth strategy.

1. Introduction

In July 2002 Nick looked pensively at the financial information in front of him (Exhibits 1 & 2). Once again he would need to raise more funds, either by attracting further business angel investment and so further diluting his equity share or by putting in extra capital himself.

Nick sat back and considered his options; had this all become too much, should he sell the business? This seemed an unlikely prospect particularly now

1. The case has been prepared by Robert Brown, Visiting Fellow, and Dr Stephanie Hussels, Lecturer in Entrepreneurship, at the Bettany Centre for Entrepreneurial Performance & Economics with help from the MBA students Philip Irvine, Tom Keohane, Joel Leeson, David Stark, and Chris Wyper. The authors would like to thank Nick Jenkins for his generous support and kindly provided insights into Moonpig.com. The case is intended as a basis for class discussion rather than to illustrate either effective or ineffective handling of management situations.

with the vast number of dot.com failures in the market and the City uncovering that many dot.com's had been grossly overvalued. Nick had also spent 3 years working to build Moonpig and had invested a large proportion of his personal assets in the business. Was he ready to give all this up?

Especially now that for the first time since starting to trade, the business was so close to breaking even. He was certain that profits would flow after that. He was sure that his concept was sound, the level of gross margin was so much higher than that he had predicted in his original business plan. What he had not anticipated was the high level of start-up costs involved. Although sales were growing and losses were decreasing the cumulative losses had now reached £2 million. Was it the case that further investment was all that was required?

2. Nick Jenkins

Nick started his first business at university selling dress shirts with silkscreen designs such as Dennis the Menace and Tintin. This was an unmitigated disaster as he ordered 200 shirts from Cyprus in varying sizes from size 14 upwards, only to find out that most of the male population has a neck size of 15½" - 16½". It taught him a valuable lesson about stock, as he was left with a lot of unsold odd-sized shirts. He graduated from Birmingham University in 1989 with a degree in Russian, a subject chosen as he had wanted to do something different.

Despite his plan to join the British Army, Nick was offered a Sales Manager's post by a German company setting up in the Soviet Union, which he accepted. Within a year he had established, from scratch, a thriving sales operation with several staff. In 1991, he was head hunted by Marc Rich and Co, to start a sugar trading operation in Russia. Within two years, the Moscow operation was making several million dollars annual profit by importing raw sugar to the Ukraine, refining it in under-utilised Ukrainian sugar factories and selling the resulting white sugar to regional Russian wholesalers. In 1993, there was a management buyout of Marc Rich & Co and Nick was one of the managers with an equity participation in the new business, Glencore International AG. The proceeds made him a millionaire at the age of 26. Typically modest, he attributed this to a great deal of luck and being in the right place at the right time to exploit the opportunities presented in Russia. After 1996, business started becoming a great deal more competitive and the Russian mafia became involved. This was a result of Nick discovering that a Siberian warehouse owner had stolen 10 million dollars worth of sugar, a detail which when Nick repeated it to the police resulted in a death threat being pinned to his front door[2]. He realised it was time to leave as it left a "rather nasty taste in the mouth"!

2. See Real Business, November 2005, p.33

For the period of 1991-1997 the net profit under Nick's direct management was in excess of $20 million. He had recruited and retained a happy and motivated team of over twenty employees in the Commonwealth of Independent States (CIS) and staff turnover from 1991 to 1997 was almost zero, in stark contrast to the situation among the competitors. Selling his interest in Glencore International left Nick with considerable funds to invest in a new business. Nick spent a year at University on the MBA course, graduating in September 1999. He immediately started work on Splat.com.

3. The Idea for the New Business

During the MBA course Nick's business ideas had included corporate gyms in the City, growing exotic mushrooms, internet based language training and greetings cards. Having narrowed the choice down to an internet business, his guiding principles were that he wanted to sell a product but not hold any valuable stock. He wanted to use the internet to produce a physical product which was an improvement on the high street version in order to avoid the otherwise inevitable price comparison. The main benefits of cards were quick order fulfilment and delivery through the letterbox, no stock requirement other than paper and ink and most importantly the added value of personalisation justified a significantly higher price than the un-personalised high street equivalent. This encouraged him to settle for cards. The complete concept was forged during his MBA in 1998/99 when he wrote a business plan for Splat.com. (See summary, Appendix 1). The name Moonpig was chosen ultimately when Nick discovered that Splat was already an internet registered domain name. Nick knew that this business would be spread by word of mouth and he needed a fun, memorable, phonetic, two syllable .com domain which could be easily represented graphically. It also needed to be unique on Google so that customers could find it easily. After several days of brainstorming and checking availability Moonpig was the best candidate. Moonpig had been Nick's nickname at school.

4. Forming the Business

Nick, while having no experience of Internet based industry except through his knowledge gained on the MBA program, compiled what he hoped would be a sustainable business model for Moonpig: holding no stock except white sheet card, receiving cash on order, ensuring logistics handling costs were negligible, and by ensuring that the cost of the last mile was low as the product was small enough to deliver through the letterbox at any time of the day.

In September 1999, prior to committing to the idea, Nick confirmed the viability of Moonpig in a meeting with Louise Tighe, MD of Paperlink Cards.

Louise, having a substantial knowledge of the greeting cards industry, confirmed that Paperlink would be interested in getting involved by offering the use of their designs on a royalty basis and also advertising Moonpig on the back of the cards Paperlink sold. (See Appendix 2). In return for this assistance Nick set aside 15% of Moonpig's authorised share capital of 100,000 shares for Paperlink to buy at the nominal price of 1p per share once they had satisfied the criteria of distributing 4 million of their own cards carrying the Moonpig.com logo. Having Paperlink's backing, Nick became confident about the idea and committed to the start-up straight away.

Nick realised that he would have to prove that his concept was viable, profitable and that he was totally committed to the business before potential investors would consider investing in the start-up. In December 1999, he loaned the company £160,000 to set the business up and provided a guarantee to the bank of another £200,000 in order to secure an overdraft facility.

Moonpig was formed as a limited company in that month and Nick immediately commissioned an IT consulting firm to begin work on the website, which was due to take 1 month. In the same month, Nick bought a property in Fulham, ensuring it was within cycling distance of his home and that the heavy-duty printers would fit through the 2.5 metre wide front door. In order to improve cash flow the printers were leased to the business. He also hired an assistant and a graphic artist. Hiring staff at this early stage placed a great salary burden on the company, as trading was delayed as a result of the website not being completed on time and the printing equipment also arrived late, being brand new models.

Nick had taken the decision to lease rather than buy the specialised digital printers he required. Lease payments amounted to £5,000 a month. Nick could also have outsourced the printing but he felt that this option would not ensure the required level of quality control; no supplier was offering this concept in the market and it was going to be more cost effective, with future economies of scale, to undertake the printing in house.

5. Launching the Business

In April 2000, after the first digital printer arrived, Nick held a launch party for journalists and friends to make the website and concept known. It was, in retrospect, a launch too soon. Chelsea FC were playing at home that evening, meaning many guests were blocked in traffic and forced back in dismay. With the venue's computer terminals crashing and only becoming operational later into the evening, nonetheless when Nick finally displayed his website, his guests loved the concept and ordered many cards. To Nick's horror, the next day he discovered that his website had crashed and he had lost all the previous night's orders. He had no choice but to send apologetic emails to his customers and hope that not too much damage had been done.

In July 2000, Moonpig began trading in earnest. Nick had hired an IT programmer to rewrite the website after having committed £100,000 in fees to the previous consultants who had nevertheless produced an unsatisfactory end product. By this stage, having paid salaries to staff for 8 months with the business not up and trading, Moonpig was facing financial strains.

To meet these financial demands, and having a location, website, equipment and crew to display, Nick felt that he was now ready to approach potential investors for funding. The deal with Paperlink enhanced Nick's credibility with potential investors as did the fact the he had invested £160,000 of his own personal money into the business. On going out to the market for funds, Nick became aware that venture capitalists were only interested in investing in business operations that required finance of over £1million. He also quickly realised that venture capitalists or investors were only comfortable in investing in businesses that had high potential for scaleable growth and this meant that he had to present a credible management team. So by the end of 2000, Nick had hired a team of staff namely an assistant, three graphic designers, a production manager, a marketing director and two assistants, an IT director, three customer service personnel and a software developer.

6. Finding Business Angels as Investors and Board Members

In the very early stages two old university friends had wanted to invest £75,000 in Moonpig and Nick had structured a deal which saw their money lent to the business on an interest free three year term alongside an issue of shares at a nominal price. They were both experienced investment professionals and able to sustain the loss so Nick agreed on the agreement that if the money was lost they wouldn't let it get in the way of friendship.

Soon afterwards Nick was looking to obtain an additional £400,000 and he decided to approach business angels. Profiting from investors' enthusiasm for the "internet boom", Nick succeeded in convincing David Noble to put the first external equity of £50,000 into the company at a share premium of £12 per share, both agreeing that the company had enough momentum to justify a valuation of £1.2 million. David had experience of running small supermarket groups and he liked the absence of "stock" in the Moonpig concept; he was also happy to become a Moonpig non-executive director.

In early 2000, therefore, the company's share capital structure was as follows:

Owner	Loans	Equity	Shares Issued	% Equity
Nick Jenkins	£160,000	£739	73,900	70%
Paperlink		£150	15,000	15%
Friends	£75,000	£50,075	15,300	15%
Total	£235,000	£50,964	104,200	100%

Nick then raised further major investment from a group of angel investors at prices between £12 and £25. Their introduction came about randomly. One of the two friends who had lent an initial £50k had previously worked for 3i and he introduced Nick to the group. The deal was too small for 3i but they recommended an angel investor who in turn recommended a further business angel - Tom, a former investment banker and media expert, who invested and introduced a further 6 investors into Moonpig. As business angels typically only invest up to £200,000 in a project, the business angels altogether raised £500,000 with Tom becoming a non-executive director.

One of the angels was also an investment director for a Guernsey based venture capital (VC) fund. Nick, while increasing his own personal loans to the company, arranged in 2001 that the VC company invest £720,000 in Altergraphics – (the VC having requested a "more serious company name" as a condition for their investment). Thanks to the Angels, therefore, the Moonpig brand name had acquired venture capital backing.

The VC investment, at a share price of £26.80, valuing the company 'post money' at £5.9 million, was based on two main conditions:

1. Nick would convert his loans and guarantees to equity at the same share price.

2. If the business failed to meet the projected sales, more shares would be issued to the VC to bring the effective valuation down to £2.2 million.

As the sales figures for 2001/2 failed to meet the target, this revaluation clause was invoked, with the resulting distribution of shares:

March 2001	**Loans**	**Equity**	**Shares Issued**	**% Equity**
Nick Jenkins	£260,000	£356,000	91,318	41%
Paperlink		£150	15,000	7%
Angels		£540,000	26,120	12%
Friends	£75,000	£50,075	15,300	7%
VC		£720,000	74,880	33%
Total	£335,000	£1,666.150	222,618	100%

The management team was completed in early 2002 when a non-executive Chairman, a former VP at Hallmark Cards was appointed, following a personal introduction to the company by David Noble. The Chairman had earlier sold his own greetings card business to American Greetings and was willing to be an angel investor as well.

7. Pricing Policy

At the same time Nick also re-evaluated his business model, as with the present gross margin, he could not cover his costs. At the suggestion of one of the non-executive directors (David Noble), Nick raised the price of the cards from £1.99 to £2.99 per card. Nick felt this price might be too high for a greeting card but the increase was vital to enable the business to meet the costs involved. However, no decline in sales was observed and of course the gross margin had soared. A 66%% gross margin (i.e. a selling price of £2.99 versus costs of £0.99) would now be achieved and all he needed to reach break-even was an increase in sales!

8. Marketing the Business

Initially in July 2000, Nick had undertaken a marketing campaign based on direct mail and online marketing. He had originally budgeted to spend £1 on marketing per customer, however, direct mailing was costing £28, banner ads £100, and buying email lists £33 to acquire a customer. With the average customer's spend being £20 per year of which £10 was gross margin, (before the price rise mentioned above) these marketing and customer acquisition costs were extremely expensive and were crippling the business. Other marketing spend was also not attracting customers with direct mail only reaping a 5% response rate. A decision was therefore taken that during 2001 no further money would be spent on marketing. Figures for the year, however, revealed that a customer growth rate of 150% had been achieved. This was believed to be viral growth achieved by word of mouth and from good PR coverage in journals such as The Daily Telegraph which Nick's PR agency had successfully created.

New marketing ideas were also being pursued. An agreement had been reached with Vodafone to send their customers greeting cards. While business-to-business marketing was not Moonpig's core activity, it brought in much needed income and assisted in building the awareness of Moonpig in the UK. In addition, an affiliate deal was undertaken with Microsoft Hotmail.com for advertising space within their sites. Obviously, the worldwide presence of Microsoft gave greater exposure than had been available previously.

As a result, by March 2002, customer numbers had increased from 15,000 to 30,000 in the last 12 months, with the strongest sector being the 25 to 36 age group, proving to Nick that "Moonpig offered a level of personalisation that it was impossible to replicate in a shop". The spread of broadband technology also helped, but most customers continued to subscribe during office hours! No serious direct competitors had appeared. On Valentine's Day, 2002, the Moonpig site had 30,000 visitors alone, business to business sales were also developing, with small businesses in particular sending personalised cards to customers and employees.

9. Decision Time

Prior to further fund raising, cost cutting began in earnest. The in-house software team was used to develop software for other people such as writing a website for a publishing company. The result was that in the first full year of taking third party contracts, the software team was able to almost pay for itself, making the work that they did for Moonpig practically free.

With the increase in sales, however, cash was still very tight. But Nick was temporarily unable to raise further finance due to the anti-dilution clause in many of his investors' Heads of Terms contracts. What this term meant was that if any further investors came into the business at a lower share price than the previous investors, the management would have to make up the difference in shares. With the internet "boom" now well and truly punctured this effectively acted as a barrier to further investment, and Nick was forced to wait until April 2002 when the clause lapsed with the publishing of the company accounts.

To add to Moonpig's difficulties, the VC firm announced that not only would they not invest in any further rounds of investment, they would rather liquidate their shareholding altogether. The Chairman saw this as an opportunity to introduce a new investor who could buy out the VC fund and add the new money required.

For Nick the dilemma was finding a price which would be acceptable to the VC fund but also low enough to be attractive to the new investor. Nick had £260k in loans outstanding to the company which he was prepared to capitalise at the new share price in order to maintain his own shareholding.

Nick knew that the VC would be reluctant to sell their shares unless they could recover a significant portion of their original investment and the new investor would be reluctant to invest unless he could buy a significant shareholding.

By mid-July 2002, Nick required £300K to keep the business running, but was confident that with the reduction in costs and increasing sales, revenues would finally start to outstrip fixed costs and Moonpig would have a profitable year in 2003. He revised his business plan, with new financial projections (Exhibits 1 & 2). The company remained focussed on humour cards in the UK. The business had absorbed nearly £1.7 million in cash, yet Nick was convinced the company needed one 'final' push to become profitable. Surely this was now the way forward, but how to price new shares remained a major issue! And should he expand internationally following enquiries from Australia and North America to franchise his concept? Big decisions indeed were required for Nick and his Board, particularly as the support of 95% of shareholders was necessary to authorise the issue of new shares.

Exhibit 1: Profit and Loss Projections

PROFIT AND LOSS PROJECTIONS - ALTERGRAPHICS LIMITED (year end 30 April)

	ACTUAL Yr 99/00	ACTUAL Yr 00/01	PROJ Yr 01/02	PROJ Yr 02/03	PROJ Yr 03/04	PROJ Yr 04/05
INCOME						
Moonpig internet sales	0	76,018	286,269	1,029,000	2,500,000	4,000,000
Moonpig non internet sales		19,929	43,598	280,000	250,000	400,000
Non Core Revenue	0	0	94,688	75,000	75,000	75,000
	0	95,947	424,555	1,384,000	2,825,000	4,475,000
DIRECT COST OF SALES						
Moonpig internet sales	0	40,114	118,885	446,345	875,000	1,400,000
Moonpig non internet sales		10,750	19,982	132,881	87,500	140,000
Non Core	0	0	19,977	0	37,500	37,500
	0	50,864	158,845	579,227	1,000,000	1,577,500
Gross Profit (Loss)	0	45,083	265,710	804,773	1,825,000	2,897,500
OVERHEADS						
Marketing						
Promo costs(Internet sales)	31,995	139,597	72,336	81,000	81,000	100,000
Promo costs (non internet sales)		0	19,377	5,000	5,000	5,000
Promo costs Reprographics		0	3,954	0	0	0
Marketing salaries		122,926	74,286	38,624	38,624	38,624
Product development salaries		19,812	24,079	24,079	24,079	24,079
Customer service salaries		19,819	45,918	45,918	45,918	80,000
Misc		4,405	3,886	2,400	2,400	2,400
	31,995	306,559	243,838	197,022	197,022	250,103
Reprographics						
Printing Equipment Depr.	0	36,542	61,269	51,130	51,130	51,000
Repro Maintenance	0	0	544	0	0	
Salaries	27,938	73,463	89,908	87,900	87,900	87,900
Repro Misc	4,072	8,135	866	1,200	1,200	1,200
	32,010	118,140	90,775	89,100	89,100	89,100
IT						
Computer hardware depr.	7,924	60,911	85,040	71,260	71,260	71,000
IT infrastructure	6,656	52,858	47,015	26,400	26,400	26,400
Salaries		99,847	132,118	132,000	132,000	132,000
IT Misc		12,935	421	1,200	1,200	1,200
	14,580	226,551	264,594	230,860	230,860	230,600
Admin						
Salaries	16,949	129,263	37,107	70,600	90,000	90,000
Admin Misc	9,473	867	979	0	0	0
Legal		71,689	9,762	3,000	3,000	3,000
Accounting		19,146	8,173	3,000	3,000	3,000
	26,422	220,966	18,914	6,000	6,000	6,000
General						
Rent & Rates	6,774	47,130	58,123	57,600	57,600	57,600
Electricity & Utilities	8,077	10,180	5,682	3,600	3,600	3,600
Insurance	999	3,237	8,949	9,600	9,600	9,600
Telephone	6,410	13,054	7,373	1,560	1,560	1,560
Admin postage & couriers	1,911	3,430	1,172	720	720	720
Recruitment fees	32,589	37,314	2,700	0	0	0
Consultancy fees	23,524	2,915	0	0	0	0
Interest payments		32,977	27,412	25,800	25,800	25,800
Bank charges	427	2,588	2,229	2,400	2,400	2,400
Stationary	6,568	7,363	4,259	2,400	2,400	2,400
General Depreciation	26,030	55,518	16,111	13,416	13,416	13,416
Misc	1,516	5,513	0	0	0	0
	114,825	221,219	134,010	117,096	117,096	117,096
Total Overheads	219,831	1,093,435	752,130	640,078	640,078	692,899
NET PRE TAX PROFIT / (LOSS)	-219,831	-1,048,353	-486,421	164,695	1,184,922	2,204,601
CORPORATION TAX		0	0	0	0	593,873
POST TAX PROFITS	-219,831	-1,048,353	-486,421	164,695	1,184,922	1,610,728
RETAINED PROFITS	-219,831	-1,268,184	-1,754,604	-1,589,909	-404,987	1,205,741

Exhibit 2: Balance Sheet

BALANCE SHEET	Yr 01/02	Yr 02/03	Yr 03/04	Yr 04/05
Fixed Assets				
Furniture & Fittings	£10,649	£7,987	£5,990	£4,493
Copyright & Licences	£23,355	£17,517	£13,137	£9,853
Printing equipment	£168,045	£126,034	£94,525	£70,894
IT Hardware & Software	£121,607	£91,205	£68,404	£51,303
	£323,656	£242,742	£182,057	£136,543
Current Assets				
Stock	£18,811	£25,000	£40,000	£40,000
Trade Debtors	£28,421	£30,000	£40,000	£40,000
Other Debtors	£1,434			
Prepayments	£10,386	£20,000	£40,000	£40,000
Bank & Cash	£18,662	£525,177	£1,494,957	£3,151,199
	£77,713	£600,177	£1,614,957	£3,271,199
Current Liabilities				
Bank Loans	£130,000	£130,000	£0	£0
Trade Creditors	£56,839	£100,000	£200,000	£200,000
VAT	£14,567			
PAYE & NIC	£9,814			
Finance Lease Creditor	£60,000	£60,000	£0	£0
Wages Control Account	-£1,500			
Directors Loan Account	£59,803			
Other Loans	£0			
Accruals and deferred income	£18,840			
	£348,364	£290,000	£200,000	£200,000
Long term liabilities				
Printer Finance Liability	£65,828	£65,828	£0	£0
Long term Loans	£75,000	£75,000	£0	£0
	£140,828	£140,828	£0	£0
NET ASSETS	**-£87,822**	**£412,091**	**£1,597,013**	**£3,207,741**
Capital and Reserves				
Share Capital	£1,682	£2,000	£2,000	£2,000
Share premium & reserves	£1,665,100	£2,000,000	£2,000,000	£2,000,000
Retained Profits B/F	-1,268,184	-1,754,604	-1,589,909	-404,987
P&L account	-£486,421	£164,695	£1,184,922	£1,610,728
SHAREHOLDERS FUNDS	**-£87,822**	**£412,091**	**£1,597,013**	**£3,207,741**

Appendix 1: Splat.com – Business Plan

Executive Summary

Splat.com is an internet retail outlet for greetings cards that uses a new digital print technology to print each card to demand. A customer accessing our web site can choose from a large range of well known cards, personalise the message or caption and have the printed card delivered to them by first class post or direct to the recipient.

1. Potential market growth from zero to £75 million by 2009

The global market for greetings card is over £10 billion and the UK represents over £1 billion alone. 30% of this value is in premium cards costing over £1. The market for greetings card sold online in the UK could grow from zero today to £75 million within ten years. The product is relevant throughout the English speaking world, and there is little problem with developing foreign language versions of the card designs. There are now 9 million people online in the UK and this is expected to rise to 25 million. Online spending in the UK is still only 0.02% of GDP at present but could rise to as much as 20% GDP within ten years.

2. Competition

Electronic Greetings

There are plenty of e greetings sites, where images can be elected edited and sent as e greetings to a recipient for free. While this is popular it can't replace the physical item and because it is quick and free is doesn't say much for the senders depth of feeling for the recipient.

Online retail of physical cards

Cybercard

Cybercard.com, based in Cambridge is the only UK based internet retail outlet. However it is also a publisher and so only sells its own products. They do print to order and allow personalisation of cards online, however the quality of the designs, card and printing leaves much to be desired. They have relied entirely on owning the greetingscards.com domain name in order to bring in custom. They have no marketing effort whatsoever and while they have been operating for several years they are only selling 10 cards a day.

Sparks.com

Sparks.com is the most serious contender. It is an American internet start up, backed with $3 million of venture capital. Sparks are a pure retail outlet selling publishers designs. Their model however does not print to demand and there is no personalisation involved. They carry large volumes of stock.

3. The product

Splat.com has three advantages over the current retail model:

- The ability to edit the caption on the front and inside the card.
- A much greater range. There is no minimum print run and no limited shelf space.
- Convenience. Not everyone has the time to visit a card shop just to buy a card and not every corner shop sells good cards.

The card will be sent together either with an envelope to the buyer or directly to the recipient.

Pricing

To buy a similar card in a retail outlet would cost from £1.50 to £2.00. The price of a Splat card delivered direct is £2.34 including VAT. There is no direct competition offering branded cards with personalisation. Good cards and good designs are not a commodity, there is no point in trying to undercut physical shops. The product is different.

Promotion

An internet site without promotion is like opening a shop without a shop front. Some customer will stumble across the web site by accident on a search engine, but this will never bring in much business on its own. All the net revenue will be reinvested in promotion until the business is ready for trade sale.

The bulk of the promotion for Splat.com will come from giving away a majority stake of the company to a leading independent card publisher such as Paperlink in return for an agreement to add the web-site address to the back of every greetings card they sell through normal retails channels.

Paperlink sells several million cards a year. They are bought by the very people Splat wants to target. They buy premium cards, and they like original ideas. We will put a simple message on the back of these cards.

Website name

Most of the generic domain names are already owned, such as greetingcards.com/ cards.com (Hallmark), greetingscard.com (Cybercard). The name of the website needs to be memorable and not easily confused. Splat is monosyllabic and the spelling is straightforward. This makes word of mouth recommendation easier.

4. People and management

The only full time staffing requirement is for order takers who would be paid on an hourly basis. I have allowed for a cost of £8.00 per hour. This is quite high for what appears to be a simple task but the job requires a special type of person who can stuff envelopes for seven hours and not make mistakes. Because the work is out of hours it is better to pay extra for a trusted long term employee. Quality and accuracy will be essential in the early years in particular.

The other tasks to be performed are settlement of royalty payments, ordering stock and preparing accounts. This would require a part time administrator on a salary of £30,000 per annum pro rata. These costs are included in the cost of general administration in the table of costs. Once sales reached 600,000 per annum this task would become a full time job.

I would handle negotiations with new publishers and general management until the volumes justified a full time Managing Director.

Management

Nick Jenkins is 32 years old and graduated from Birmingham University with a degree in Russian Language and History. Nick spent eight years in Russia setting up and running businesses for Glencore International AG, a large Swiss commodity trading company. In 1998 he came back to the UK to study for an MBA.

Nick will be the Managing Director of Splat.com.

Robin Stevens is 32 years old and is the managing director of Fourth Day New Media, an e-commerce strategy consultancy. Among his clients are McKinsey & Co and the National Health Service. He has spent four years in the e-commerce business following a career in advertising.

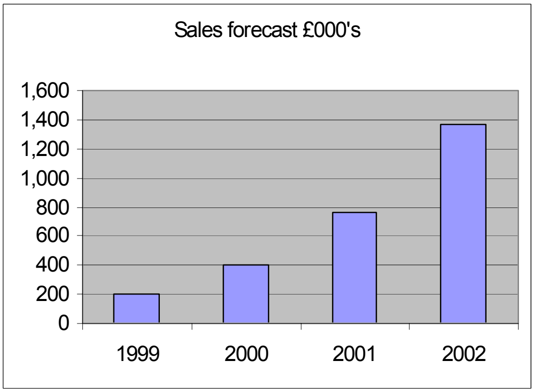
Robin will act as a consultant to the business in return for an equity stake to be agreed. This is in addition to the work carried out by Fourth Day on the setting up of the web site which will be paid for by Splat.

5. Very low fixed costs – highly scaleable

After the initial sunk development costs of £50,000 almost all costs are variable. The business costs less to set up than putting out a single retail unit and yet it can service any customer on the planet.

Sales Forecasts

It is hoped that sales will reach £1.4 million after four years. This will be achieved largely through organic growth. The company would then be in good position for a trade sale.



Assumptions Unpinning

Financial Forecasts

Our greetings card publisher, Paperlink, currently sells two million cards a year. Their customer base is made up of about 200,000 buyers each buying ten cards per year from that publisher. They send their cards to a further 200,000 recipients, some of whom may overlap. This is a combined base of 300,000. In addition there are many others that will see the cards either as they browse or while looking at friends cards on display at home.

Variable and fixed costs

Variable costs per card excluding VAT	
Card	0.10
Greeting card envelope	0.02
Despatch envelope	0.02
Printing	0.06
Postage	0.25
Labour costs	0.10
Payment processing	0.15
Royalties to publisher	0.30
Marginal costs per card	1.00
Revenue per card excluding VAT	2.00
Gross profit per card	**1.01**
Gross profit margin	**50%**
Non Volume dependent fixed costs	
Website design & maintenance	25,000
Website hosting	12,000
Domain name and search engine fees	4,000
Computer (1 year depreciation)	4,000
Volume dependent fixed costs (for 300,000 cards)	
Admin & Management	30,000
(this equates to 10p per card)	
Total fixed costs	75,000
Breakeven number of cards per year	**74,627**
Breakeven number of cards per day	**204**

The type of customer who buys these cards is 18-35, affluent, innovative and more than likely to have access to the internet. Because the advertising is so targeted we expect a conversion rate of 5%.In otherwords, in year 1, 15,000 individuals will buy cards from the site as a result of seeing the web site address on the back of cards sold through ordinary retail outlets. These customers will then return to the site to buy on average six cards in a year. These will probably be bought one by one., though hopefully some customer will stock up especially at Christmas.

In year 2 sales will be represented by:

- Retention of existing customers through a customer loyalty programme,

- Additional customer brought via advertising on offline retail cards
- Customers brought by advertising on splat online cards
- Customers brought as result of off line advertising spending.

In years 3 and 4 sales will increase for the same reasons.

Profitability

The costs shown in the table overleaf do not show the figures spent on advertising. While any surplus may be used for advertising and promotion in the first four years the underlying profitability is close to 40%. There are very few overheads except advertising. In the long run the need to spend on advertising will diminish.

Variable costs

90% of the total variable costs are only incurred if an order is made. All of these costs bar postage will reduce with volume

Fixed costs

The initial development will cost £46,000 before the first order comes in. The administration and management costs will be incurred as the business grows.

Cash flow Forecasts

Once the business breaks even the cashflow will be positive. Since sales receipts are received immediately and royalty payments and suppliers invoices are settled at 30 days a boost in business could not cause a cash flow problem. There is no danger of over trading.

Cashflow forecast					
	Units (000)	Sales £000	Overheads	Variable costs	Cash available
Year 1	100	200	75	100	**26**
Year 2	200	400	75	199	**126**
Year 3	380	760	83	378	**299**
Year 4	684	1,368	113	681	**574**

The cash available can be reinvested in the business.

Balance sheets

This is not a capital intensive business. The computer involved is capable of handling almost any volume of business. There is no stock required other than 9 weeks' blank card and envelope stock.

Breakeven analysis

The business needs to sell 75,000 cards a year to break even.

Burn rate

With the promotional scheme envisaged, the cost of marketing is paid for largely by giving away equity. If business is slow to develop, the cost of maintaining the business without sales is less than £1,500 per month. With every internet based product there is an ideal time to go to market. Many companies have suffered from ploughing too much money into a product before the online market was ready.

6. Financing requirements

Shareholders

First round

The business will be set up as a limited company. The shareholding structure would be

Shareholder	Contribution	Holding
Nick Jenkins	Development costs and working capital (£50,000)	>50%
Card publisher	Advertising and industry advice	<50%

From a publishers point of view this is a good deal. It costs them nothing and it means that they will benefit from the sales of other publishers cards on the site.

The deal with the publisher has yet to be agreed. In order to secure the agreement they would need a high enough stake to make it interesting to work with Splat rather than attempt this by themselves.

The initial development costs are already secure. It is quite likely that more funding will be necessary once the site is up and working in order to speed up the promotional effort. I envisage that this would be within six months of start up.

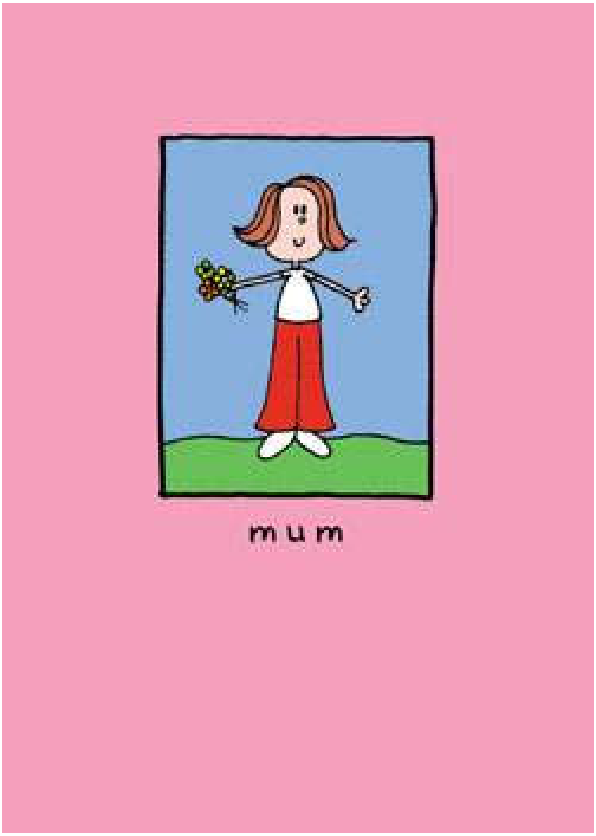
Second round

If a cost effective form of promotion can be found that would significantly increase growth then a second round of financing may be sought at the end of year 1, when the site has been operating for long enough to prove the model.

Exit routes for investors

The aim is to exit before the end of year four though a trade sale to a large greetings card retailer such as Hallmark or Clintons cards. Once the business model had been proved and the company has become well known it would be easier for them to buy Splat than try to replicate it. In the internet business, gaining market share is crucial and there will only be a short window of opportunity in which to do it.

Appendix 2: Example of customised Greetings Cards



Happy Birthday Alexandra

HELEN FINALLY FOUND A CURE
FOR DAVE''S SNORING.

Marketing Message on back of Paperlink cards

off beat

humour from Paperlink

OF049 True Self

Chris Madden, colours by Jenny Gordon

Customise this card online at...

www.moonpig.com

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price code FF 40

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