Developing a financial plan for investment that inspires confidence

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Reading time 9 mins

Key Points

- When pitching for or submitting proposals for investment, developing a financial plan is crucial to success
- Investors need to know that you have an exit strategy and feel confident that you're worth the risk
- A clear financial plan should include your income statement, cash flow projections, balance sheet, sales forecast, and a spending strategy regarding what you plan on doing with their investment
- Articulating the type of investment you need is clear – especially if it's not necessarily money that you need
- Use free templates and toolkits for small businesses or creative enterprises to help you get started

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Poor money management, overspending on inventory, and not developing a clear financial plan are key financial mistakes entrepreneurs make when seeking investment. You need to demonstrate that you have a good understanding of the business side of your product's market potential to make it easier for investors to feel confident that they'll get their money back. When developing a financial plan for investment proposals or when pitching to investors, ensure that you've covered the essentials and can confidently explain your:

1. Income statement
2. Cash flow projections
3. Balance sheet
4. Sales forecast
5. Spending strategy on investment

Developing a financial plan for investment and drawing up financial statements can be a difficult and time-consuming task. So much so that many innovators and entrepreneurs avoid giving it their full attention. Using the services of a professional is an option that those with sufficient startup capital might choose. However, understanding key terms (e.g. turnover, margins, gross and net profit) is an essential part of finding investors for your product idea – especially when giving presentations in person and have one chance to inspire investors with confidence!

Financial plan essential #1: Income statement

Also referred to as a Profit and Loss (P&L) Statement, the income statement is one of the core financial statements your business needs to be able to provide. Profit or loss is determined by taking all the revenue over a defined period (e.g. over an annual cycle) and subtracting all expenses from both operating and non-operating activities. It can be as detailed as you want – but your income statement must include:

- Revenue: Also known as gross sales and is the total amount generated by the sale of goods and services
- Cost of revenue: The total cost of manufacturing and delivering the product or service, including indirect costs (e.g. distribution and marketing)
- Cost of goods sold (COGS): Also called the cost of sales, and is all the direct costs associated with making the product. It will include all direct costs (e.g. labour, raw materials), but none of the indirect costs
- Goss profit: Also referred to as gross income and is calculated by subtracting the COGS from revenue (sales)
- Gross profit margin: Commonly used to measure profitability, as higher margins usually mean bigger profits. It's the profit margin that tells investors how much a product makes when all of the direct costs have been subtracted

- Operating expenses: The costs you paid (e.g. wages, rent, utilities) to generate the revenue
- Operating income: What's left over when operating expenses have been deducted from gross profit
- Earnings before taxes (EBT): The money left after all expenses and losses have been subtracted from revenue and gains
- Net profit: Also called net income, and is what's left over once everything has been paid

Financial plan essential #2: Cash flow projection

Your cash flow forecast details how you expect money to flow into and out of your business, make money, and pay your bills. It's an essential tool to manage your cash flow and prepare for months when you'll turnover more or less (e.g. Christmas). Prepare your forecast by:

- Planning as far ahead as you can accurately predict. If you're a new business, you might not have enough data to forecast accurately: gather as much industry/sector data as you can to help you make reasonable predictions
- List all your forecasted income: For all the weeks or months you're indicating, list all the cash you've got coming in: this includes sales, client payment dates, royalties or licensing fees, tax refunds etc.
- List all your forecasted expenditure: For each of the same weeks or months, how much will you spend, and on what? This includes rent, salaries, marketing, taxes, bank loans and fees
- Calculate your operational cash flow: Subtract your expenditure from your income and get your cash flow figure. Keep a running total for a clear picture of your cash flow forecast over time that you can use to help make informed business decisions.

When you're developing a financial plan for investment, your cash flow projection is essential to getting potential investors excited – or making them nervous! Too many weeks or months with negative operational cash figures spells trouble. However, consistent periods of positive cash flow could be a good signal for expansion.

Financial plan essential #3: Balance sheet

A balance sheet gives investors insights into your company: its operations, assets, liabilities, and equity structure. Key information includes:

- Assets: Anything the business owns (e.g. property, vehicles, equipment), including the revenue you expect to take (accounts receivable)
- Liabilities: The revenue to expect to spend (accounts receivable)
- Equity: How much equity the owner has, as well as other investors or shareholders

It’s called a ‘balance’ sheet because the equation must balance out:
Assets = Liabilities + Equity

Financial plan essential #4: Sales forecast

This is arguably the most important part of developing a financial plan, as it predicts how much you plan to sell over a given period. It’s an ongoing part of your business planning process and should be consistent with the sales number used for your income statement. One way to calculate your sales forecast is to:

1. Quantify the estimated sales volume over a given period (e.g. 1000 in June)
2. Define the unit price (£10)
3. Multiply the estimated sales volume by the unit price (£10,000)
4. Calculate the cost of sale and multiply this by the estimated sales volume (£3 x 1000 = £3000)
5. Subtract the total cost from the total sales (£3000 – £10,000 = £7000)
6. Sales forecast for June = £7000

Even though this is an estimate, be as accurate as possible. Divide your forecast into segments and forecast for each segment separately. For example, if you’ve got an ongoing order/sales contract with a specific client, that would be a separate segment from predicted online sales on Amazon or Shopify.

Financial plan essential #5: Spending

strategy on investment

By the time you get to this point, you should be able to confidently demonstrate your product's business viability, market opportunity, and ability to manage finances. If your product is doing well, investors will want to know why you need the money. If you're still in the early stages of product development and don't necessarily have the sales numbers to back your projections: why should they take a risk on you? More importantly, this is another opportunity to woo investors with your business acumen and goal-oriented insights and inspire them with confidence in you and your product.

If you've researched potential investors and the type of investment you need – we hope you have! – then perhaps you've concluded that money isn't what you need. An important part of developing a financial plan for investment is being clear about where you're going and what you need to get there. This could be marketing expertise, distribution and retail contacts, or help with breaking into foreign markets. The ability to eloquently articulate these needs is vital to finding the investment partner of your dreams.

Our final thoughts on developing a financial plan for investment

Take your time, and do it right. As entrepreneurs focused on the exciting world of innovation and product development, we're not naturally inclined to speak in terms of forecasts, profit margins, and balancing spreadsheet equations. More importantly, many aspiring entrepreneurs fail to explain to potential investors what their exit strategy is (i.e. how and when they'll get their money back). However, if you're looking for investment, finance is a language you need to speak…Not fluently, perhaps, but enough to comfortably communicate so that your partners can feel confident you won't get lost.

If you're just starting out, look for free resources such as Nesta's Creative Enterprise Toolkit to help build the framework for your business and develop a financial plan for investment. Subscribe to our newsletter for notifications on the rest of the articles in this series, and feel free to let us know how you get on!

Comments

We love to talk about new ideas

Do you have an idea? Book a consultation with an expert - it's free, it's confidential and there are no obligations.

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