Technical Assistance Facility (TAF) for Industrial Modernisation and Investment

TOOL #5 Basics of financial planning

Sources of revenues, sales (distribution) channels and cost structure

What is the tool about?

A project finance model **allows you to assess the economic feasibility of a project.** The **model is based upon the projected cash flows of the project,** making **the latter feasible only when financially sustainable**, namely when capable of producing enough cash to cover all operating and debt-servicing expenses. Finance modelling requires the definition of some preliminary components, including the identification of the project sources of revenues, the establishment of the price at which the product/service will be offered on the market, and the estimation of the total funds needed to complete the project.

Why is it important?

Your offerings and business model **needs to be financially sustainable.** One way to ensure this is the **case is assessing its economic feasibility** through the **basic financial modelling** at early stages of the project development, which will give **the preliminary indication of its financial readiness.** The financial modelling shall focus at the short-term and long-term projections to cover the entire project development and implementation cycle. Therefore, this assessment shall provide the estimate of costs and sources of revenues as well as to provide the indication of the funding needs and matching financing sources.

Checklist/key steps:

- **Budgeting and forecasting** is the first step in developing the financial projections and it provides preliminary indication on the financial position and future financial performance (it is typically used to predict future revenues, expenses, and capital costs). There are different budget and forecasting models that can be used as a base and "translated" into excel sheets for continuous updating. This type of an exercise will help you to develop deep understanding of project/company current needs as well as key trends and assumptions that might impact its future performance.
- **Identification and estimation of key resources for the project implementation**: financial projections do not only imply to the revenues and costs. The estimation of the key resources needed for the project implementation such as natural (land, raw materials), labour (human), capital (machinery, factories, equipment) are very relevant elements that have to be identified at early stages of the business planning and as such to be included in the financial projections.
- **Adoption and validation of the sales strategy:** service and product offering are the base of your business model, thus the sales strategy shall be developed and validated at early stages of your project development. This milestone can be achieved through partnering with clusters, incubators, accelerators, and similar entities and can help with identifying your distribution channels. The sales strategy is an important element in defining the revenues sources and the cost structure, including the cash flows.
- **Presenting the investment proposal to financial institutions/intermediaries/investors:** the best way to validate your financial projections is to present them within the scope of the investment proposal to the relevant financial institutions such as commercial banks or some other financial intermediaries and/or to public/private investors. Their input will provide the valid feedback on the credibility of the investor/financial readiness of your proposal that will help finalising it.

Methods

There are different approaches and techniques used for financial modelling depending at which stage the projections are made. Most of the methods can be easily applied in excel and from there further updated and upgraded throughout the process. Since financial projections are the basic part of the business modelling, the eFinancialModelsCanvas method is a good base to start with as it helps to analyse business from a financial modelling point of view. Read more about this method here. The financial modelling examples can be based on different models, from financial statements (balance sheets) and forecasting to merger and acquisition model (M&A), asset and liability financial models (ALM), capital budgeting, IPO model and others. More in-depth financial projections may require accountancy and financial analyst skills, therefore, the expertise in the field and the knowledge on the most appropriate financial modelling methods to be used correspondingly. Some of the examples and the templates can be found here.

Do's and don'ts for interregional investment initiative development:

Do's:

- **seek expert advice and support** in business and financial modelling if that expertise is not available in-house as the financial projections are vouching for the economic feasibility of your project and access to further funding.
- **validate your business and financial readiness** with the financial actors, intermediaries and/or investors at the early stages of the business plan development as they can provide a valid input on the economic readiness of your business idea that will help finalising your financial/business planning. Moreover, their assessment of the business potential of your technology/product and service offering may result in securing the additional funding for your project.
- take advantage of the **complementary initiatives to build synergies** and collaboration, and access to funding.
- **engage at early stages relevant actors and end-users** to maximise the uptake of your business idea and secure customer sources and distribution channels.

Don'ts:

- **disregard early identification of the key resources** needed for the business implementation, both short and long-term;
- **disregard different project stages of development,** from the project/business plan development to the project's deployment and implementation as different stages require different type of effort and resources to which the matching funding sources shall be planned accordingly;
- **do not base your financial projections on assumptions and estimations** as they are vouching for the credibility and sustainability of your business idea and as such will be challenged by the potential partners and financial intermediaries/public/private investors you would be approaching.

Case study:

- Crystalline Nano-Silicon Powder for anodes in Next-generation Li-ion Batteries (CNS-in-LiB) from the Advanced Materials for batteries partnership
- Bi Rex project from the Chemicals partnership

More resources:

- Financial modelling tools
- How to build an integrated 3 statement financial model