Investment: A guide for sustainable energy enterprises and NGOs

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The Ashden Awards for sustainable energy

GVEP International

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Purpose of this guide

This guide provides an introduction to assist sustainable energy enterprises or NGOs that are seeking investment to start or expand their activities. By the end of this guide, you will

- Understand the financial needs of a business and why investment is necessary;
- Have been introduced to types of investment finance including debt, equity and quasi-equity and be able to decide which is most suitable for your business;
- Understand the steps required to raise investment finance; and
- Be able to look for potential investors.

The guide provides tips on writing a business plan, including dealing with carbon finance, and explains where you can find further information and sources of finance.

Introduction

Since 2001, the Ashden Awards for Sustainable Energy have been rewarding and supporting enterprises and NGOs that are delivering energy and changing lives with solar, micro-hydro, biogas, improved stoves, water pumps and other technologies. The health, well-being and poverty alleviation benefits of these technologies have been well documented, and they have the additional benefit of being low carbon, compared to traditional energy systems based on fossil fuels or biomass.

These winning programmes have demonstrated that the challenges of delivering energy to the poor, often in remote areas, are not insurmountable. They have shown that scale can be achieved and millions of people can be reached, and that profitable models are possible.

Not all sustainable energy programmes can and should be profit-making enterprises. However, there is not enough aid or grant funding to meet the needs of around two billion people lacking access to modern energy services[1], and profitable models have the potential for rapid scale-up and wide dissemination in the developing world.

Finance is one key ingredient for scaling up sustainable energy enterprises. Three types of finance are often necessary:

- Investment finance – for enterprises in the sustainable energy supply chain.
- Carbon finance – to capture the value of the carbon savings from global carbon markets.
- End-user finance – to help customers purchase energy products.

With our partners GVEP International and Arc Finance, we are preparing short guides to help Ashden Award winners, GVEP partners and other sustainable energy enterprises to negotiate these three areas.

This guide is an introduction to investment finance for sustainable energy enterprises and NGOs.

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[1] International Energy Agency, World Energy Outlook 2006 (Paris: IEA, 2006). http://www.iea.org//textbase/weo/electricity.pdf and http://www.iea.org//textbase/weo/cooking.pdf

1. Sustainable energy enterprises

1.1 What is a sustainable energy enterprise?

For the purpose of this guide, we define a sustainable energy enterprise as one of the following: an organisation which is selling products that allow customers to generate sustainable energy or to save energy; one that is generating sustainable energy locally and selling it to customers (or to an electricity grid); or an enterprise which is itself powered by local sustainable energy. We define 'sustainable energy' as energy that brings environmental, social and economic benefits – it includes energy from solar, micro-hydro, biogas, energy-efficient cooking stoves, and other technologies.

Sustainable energy enterprises might be:

- Manufacturers
- Importers
- Wholesalers
- Retailers
- Installers and service contractors
- Generators and distributors

Some enterprises may cover more than one of these (e.g. importing, assembling, retailing and installing solar home systems). Others will focus on just one element (e.g. manufacturing stoves and selling to distributors).

Like any other enterprise, a sustainable energy enterprise needs to understand its market, it needs to clearly define its customers, and it needs to provide the benefits demanded by its customers.

Many energy enterprises are not-for-profit organisations, or are subsidiaries of not-for-profit organisations. Unless they have a long term source of secure grant funding, they need to earn enough income from sales to cover their costs and make enough profit to reinvest in the enterprise and to repay investors if they have any.

SELCO India

SELCO is a private enterprise that sells solar home systems, solar lanterns, improved cookstoves and other sustainable energy products to poor communities in Karnataka, India. End-user finance is a key element of their business model – they provide loans directly and through finance partners to help their customers afford the purchase price of their products.

Since 1995, they have sold more than 100,000 solar home systems.

In January 2009, they announced a "social growth financing investment" from an international consortium of leading social investors – Good Energies Foundation, Lemelson Foundation, and E+Co.

For more information:
http://www.ashdenawards.org/winners/selco07

Zara Solar, Tanzania

Zara Solar is a company that sells and installs solar home systems and other solar products in the Mwanza region of Tanzania. Their business model is based on imports of quality solar products from around the world, and assembly and installation to meet customer needs.

Zara are building a network of dealers to increase their marketing reach, and they have started to work with local Savings and Credit Cooperative Societies (SACCOS) to sell products on credit to customers that cannot afford to make a lump-sum cash payment.

They have sold over 14,000 solar home systems.

Zara have received a number of investments from E + Co to fund their growth.

For more information:
http://www.ashdenawards.org/winners/zara

International Development Enterprises, India (IDEI)

IDEI is a not-for-profit organisation that won an Ashden Award for their treadle pump programme in rural parts of Eastern India.

Treadle pumps are a low cost product that substitute for expensive, polluting diesel pumps and can transform livelihoods for farmers by allowing them to cultivate crops outside the normal growing season.

IDEI prides itself on its application of commercial business principles in its path of socio-economic development – for example, they aim to support private companies to manufacture and market its pumps and irrigation technologies (including a spin-off company called Global Easy Water Products Private Ltd)

For more information:
http://www.ashdenawards.org/winners/idei

Gaia Association, Ethiopia

Gaia Association is a not-for-profit organisation that promotes ethanol stoves for cooking in Ethiopia. They won an Ashden Award for a partnership with UNHCR, to provide ethanol stoves to refugee camps in the north of the country.

Ethanol is produced from molasses, a waste product of the Ethiopian sugar industry, and ethanol cooking stoves can replace charcoal or kerosene stoves – with great benefits for the health of users, and for the environment.

Gaia Association are currently working with a private sector partner and investor, Makobu Enterprises, to establish a commercial business selling ethanol stoves in Addis Ababa.

For more information:
http://www.ashdenawards.org/winners/gaia

1.2 What business challenges do sustainable energy enterprises face?

Energy enterprises face a number of challenges that can make this sector different from an investment perspective.

Enterprises based on selling products may require their customers to pay a high initial cost, but then their recurrent energy costs are much lower. End-user finance is often vital for spreading the payment for those energy products over a longer period.

For example, buying and installing a solar home system typically costs at least $200 (depending on the size and where you are in the world), but will continue to provide light and electricity for many years without additional cost (apart from occasional battery replacement). This compares to kerosene lanterns that cost only a few dollars to purchase – but of course require continuous purchase of kerosene.

These product-based enterprises often need to provide product maintenance or servicing – for example by training a network of technicians that can provide maintenance and repair services to their customers. This can be expensive to set up, but without it they risk discrediting the products and destroying future demand.

Enterprises based on selling services or on selling energy do not present customers with the same challenge of high upfront costs (unless they charge high connection fees). However, the initial costs for the enterprise itself are likely to be much higher. They will require investment or subsidies to pay for construction of the generating facility and the transmission and distribution equipment before any income is generated from customers.

These energy generation enterprises are also more difficult to manage, as they have to manage demand patterns across a network of customers and maintain long-term relationships with them, rather than one-off transactions.

Finally, the sustainable energy sector has been pioneered by NGOs and other not-for-profit groups. Many successful enterprises have “hybrid” models that operate within a not-for-profit group or as a trading subsidiary of a not-for-profit. From an investment perspective, this can bring practical or legal complications in many countries (for example when selling equity shares). It also can bring challenges of culture and business experience. Thinking about investment when you have been used to working with grants may require new performance indicators, new ways of looking at the management accounts, and new ways of reporting.

2. Financial needs

2.1 Why do I need to make a profit?

Every enterprise has to make a profit. Without a profit you won’t be able to invest in growth, or to pay back investors. Growth will lead to greater confidence amongst investors, and open the doors to more investment, enabling the enterprise to expand still further.

“For me, a ‘sustainable’ enterprise means an enterprise that has a defined market, sound management practices and operates at a profit that will guarantee its survival for a long time.”

Kavita Rai, GVEP International

Remember though that profit only comes after paying all the staff as well as all the other expenses. That requires a product or service which is marketable and which you can persuade customers to buy at a price which exceeds the costs. For most enterprises, prices tend to be market-based so costs must be controlled to keep sufficiently below the price in order to make a profit.

Making a profit is just as important in a not-for-profit enterprise as it is in a for-profit enterprise. The feature which distinguishes not-for-profit enterprises is that they do not have shareholders and do not, therefore, distribute the profit. Instead, all profit is retained and ploughed back into the work of the organisation. This may also enable them to share the benefits with their customers and sell at a lower price. They need to take exactly the same care as any other enterprise to ensure that their costs are under control and that they do not make a loss.

2.2 Why do I need finance?

Apart from the simplest enterprises with customers that pay cash in advance, all enterprises need investment finance.

Enterprises need finance:

- To purchase fixed assets (equipment with a life of more than one year);
- To use as working capital, since enterprises are likely to have to pay suppliers, rents, wages and other costs before they receive the money due from customers;
- For start-up or growth periods, to cover expenditure until sales income has reached breakeven. In this case, you should do your market research and then set a price based on your forecast of likely sales and on the competition; but it may take some time before your customer base has grown to the point where the sales income is covering all the costs, so you need to be able to cover the costs in the meantime. You need to make enough profit ultimately to cover those start up costs.

2.3 I thought investment was for businesses: is this relevant for not for profits?

Yes! Many sustainable energy not-for-profit enterprises are earning income by selling products and services. Investment may help you to grow and to reduce your reliance on grant funding. The mechanics and legalities of investment in not-for-profit enterprises often depend on the country where you are and the type of investment. If you need advice, then good starting places might be social investors already investing in enterprises in your country or the Chamber of Commerce.

For example, legal requirements in some countries make it difficult to accept anything other than grant or trading income. Some investors are unable to invest in not for profits because of the way in which they are structured or because of the inability to have share capital.

Many of these problems can be overcome by using one of the ‘quasi-equity’ options described below. However, where there is already a not for profit company, it may also be sensible to create a trading subsidiary, that is, a for profit company that is wholly or mainly owned by a parent not-for-profit organisation.

2.4 What are fixed assets?

Fixed assets, or capital assets, are assets that have a life of more than one year and are generally quite expensive. This might, for example, be the equipment needed to manufacture your product or the equipment needed to generate electricity. They would also cover premises if you own them.

If you buy fixed assets, rather than renting, then some of your capital will be tied up and not available for use as working capital. You will need to make a

trade-off between conflicting requirements[2]. Spending your cash on fixed assets such as new equipment may assist you to increase sales (by producing more products or more energy) or to reduce costs (by making each product or unit of energy cheaper to produce). However, if your cash is tied up in fixed assets then you cannot use it for working capital and you could end up with cash-flow problems.

The annual 'cost' of your fixed assets is represented by the depreciation charged each year to the profit and loss account.

2.5 What is working capital?

Working capital is the money required by an enterprise to pay for supplies, salaries and overheads in advance of payment from customers.

"Working capital is an issue that young companies almost always underestimate. The entrepreneur should assume that everything they need will be funded in advance, they will hold some inventory, and customers will not pay immediately. They need to be realistic as to how much money will be needed to fund working capital and build it into the model from the start."

Rajan Kundra, Acumen Fund

For example, as a retailer or manufacturer of energy products, you will need to ensure that you have sufficient money available to cover your stock, which includes raw materials, work in progress and finished goods. Once you deliver those goods or services to your customer then you have sold them.

Receipts from your customers release cash which can be used to pay your suppliers, to pay your salaries and overheads and to provide a profit. But you may not be paid for some time. The money tied up in this way is known as working capital.

[2] This decision should also take into account the fact that long term fixed assets can also act as collateral to help borrow for working capital requirements

3. Types of finance

3.1 What kinds of finance are available?

Essentially, there are three kinds of external finance: debt, equity and grants.

There is also a source of internal finance: profits. If you are already in business, you may be able to retain some of the profit within the enterprise. This becomes part of the equity in the enterprise, though is often described as 'reserves' on the balance sheet.

3.2 What are grants?

Grants are very simply gifts of money provided to you to enable you to achieve the objectives set out in your grant request.

They may come from government or multilateral donors (e.g. DFID or the European Commission), from charitable foundations (e.g. The Bill and Melinda Gates Foundation), from corporations (e.g. Shell or Coca-Cola), or from individuals.

Grants are the cheapest form of money available, though donors and sponsors may impose specific conditions in return for the grant. However, it can be hard work if you need continually to secure grants to keep your business working especially when the providers of grant aid change their priorities.

Grant funders may be particularly unwilling to keep on providing grants where they believe that products and services can be sold profitably, though they may be willing to provide some seed capital to help launch a new product or new service or even a new business. Ultimately, relying on grants means that you are not in control of your own destiny.

Advantages for the enterprise	Disadvantages for the enterprise
No need to repay	The donor will have their own objectives, which may not be fully aligned with your organisation and so may cause "mission drift" as you try to meet them. Donation sizes are typically quite small, so you can spend a lot of time and money chasing small amounts of money, and then managing your funders. Donors usually have a limited appetite for continued funding of the same activity, even if it is successful – so you will have to keep on generating innovative ideas, or look for other funders.

3.3 What is equity?

Equity, or shareholder capital, is the money introduced into an enterprise by investors(including the founders and directors) in the hope of getting a future return. If it is a company, then the equity is introduced in exchange for shares – and investors will own a percentage of the company. If the enterprise does well, the shares attract a dividend (that is, a share of the profit) each year.

For an energy enterprise, the advantage of equity (compared to debt) is that risk is shared with the investor. If the enterprise is not successful then the money does not have to be repaid in full, and if the enterprise becomes bankrupt, an equity investor can only take a share of the assets that remain after all other creditors have been repaid.

A further advantage is that equity is more flexible than debt, because it does not have a fixed repayment schedule. Dividends are generally issued at the discretion of the directors, once the enterprise is profitable. So if the growth of revenue does not follow predictions then the enterprise will not find itself with a burden of repayments that it cannot meet.

The final advantage is that the investors are dependent on the success of the enterprise for their returns – and so they are more likely to be active in providing support to the enterprise.

However, these characteristics mean that equity is riskier for investors, and so they will look for higher returns – making it harder to attract. Negotiation and due diligence processes are also typically more time-consuming and difficult.

Equity investments may dilute the ownership of the founders and so reduce their control over the enterprise. Many equity investors request a seat on the board of the company.

Enterprises can offer different types of equity. The most important distinction is the priority that is given to the share owners in the payment of dividends or in the allocation of assets if the company goes bankrupt. The higher the priority, the lower the risk for investors – and in general investors that are taking a greater risk will want to see a higher financial return. This will be part of the negotiation with potential equity investors.

- **Preference shares** pay dividends before other types of shares, and have a priority in asset allocation if the company enters liquidation. This makes them lower risk for investors.
- **Ordinary shares** are the most basic form of equity investment and they have a lower priority than preference shares when it comes to dividends and assets.
- **Convertible debt** is a type of loan finance that is converted, under pre-determined circumstances, to ordinary shares.

Advantages for the enterprise	Disadvantages for the enterprise
Risk is shared with the investor, so investors are fully aligned with the success of the enterprise and do not have to be paid back if the enterprise does not succeed. Payback is more flexible and so a slower profit growth than projected will not cause interest payments to rack up.	Investors will look for higher returns to balance the higher risk – so equity investment is likely to be harder to obtain and will be more expensive than debt Negotiation and due diligence processes typically take longer Founders will relinquish some ownership and control to equity investors

3.4 What is quasi-equity investment?

Quasi-equity is a type of investment that aims to provide the benefits of equity financing without the complications of share ownership. It is typically offered by “social impact investors”, who are investing to achieve a combination of financial returns and social and environmental objectives.

A typical quasi-equity investment will provide an investment with an agreement to pay back a percentage of the enterprise's profits to the investor, once it becomes profitable. This "profit share" will then pay back the initial investment, plus a profit for the investor, and it may be capped at a pre-agreed amount or time-period. This gives advantages to the enterprise in that nothing is repayable until the project is successful, and to the investor in that they can share in the profits of the project.

Quasi-equity can support enterprises that are unable to raise debt, perhaps because they are too risky or they can't provide collateral[3]. It can also support enterprises that cannot raise equity, perhaps because of their legal structure or because they don't meet the criteria for equity investment. It does not dilute ownership or control in the way that equity often does and the enterprise's legal structure is not a problem.

Venturesome, an investment organisation in the UK, has developed the concept of 'revenue participation agreements', based on the idea of 'participating loans'.[4] The enterprise sells a 'Revenue Participation Right' to Venturesome for a fee, which is typically treated as income in the accounts of the enterprise. In exchange, Venturesome receive the right to a percentage of revenue for a fixed number of years. Venturesome caps the total sum payable, so if you hit their target in say three years instead of five, the right is terminated.

A "participating loan" is another type of quasi-equity financing. This refers to debt, usually interest-free; the borrower repays the loan amount (principal) in the usual way and, additionally pays a pre-determined percentage of the profit.

Advantages for the enterprise	Disadvantages for the enterprise
Provides capital investment in a very simple way Open to businesses that may have difficulty in accepting equity investments Exit and payback is clear, compared to equity Financial reward to investor is positively correlated with social success	Investors may be wary of quasi-equity because risks and financial return are not always clear Can be complex: participation (effectively royalties) may be calculated using net profit, gross receipts, net operating income, net income or net cash flow.

3.5 What is debt?

Loan capital, or debt, is money lent to an enterprise. You have to repay the capital sum and you also have to pay interest. Sometimes you may need to pay an arrangement fee.

The lender will want to ensure that you can repay the loan so will want to ensure that your expected cash flow is sufficient to cover capital and interest. Lenders will not want to lend significantly more than the level of equity in the enterprise. The ratio of debt to capital employed (that is debt + equity) is known as the gearing and banks aim to keep it below 50 per cent.

[3] Collateral is also known as security . It refers to assets, whether owned by the enterprise or by individuals, which are pledged to the bank and which may be seized by the bank in the event that you fail to repay the loan for which security has been pledged

[4] For more detailed information, see "Quasi-Equity: Case study in using Revenue Participation Agreements", Charities Aid Foundation: www.cafonline.org/pdf/Venturesome%20-%20Quasi%20Equity%20-%20March%2008.pdf

Gearing: an example

Gearing is the ratio of debt to capital employed:

$$\text{Gearing} = \frac{\text{Debt}}{\text{Capital employed}}$$

Imagine that your company has $100,000 in debt and $200,000 in equity.

$$\text{Gearing} = \frac{100{,}000}{300{,}000}$$

So your gearing is 0.33 or 33% and will almost certainly be acceptable to an investor.

Lenders will also look at lending cover, that is the ratio of net profit to interest, and will be aiming for somewhere close to four or above.

Lenders will not want to lose their money should your enterprise fail and so will generally also look for collateral (by taking a charge over assets such as property owned by the company or founders, or by seeking a guarantee, perhaps from the owners or from a parent company). This usually has to be worth considerably more than the loan. In some countries, governments have introduced loan guarantee schemes to support enterprises that have insufficient collateral of their own.

Interest on loans is usually tax deductible whereas dividends to equity holders are usually paid from post-tax earnings.

Debt is available from a wide range of organisations including banks, micro-finance institutions, and even from your suppliers. It can take a number of forms:

- **Bank debt**, for example an overdraft or a term loan (debt with a fixed loan period) arranged with the bank. This can be cheap and accessible, but it usually requires a guarantee and a track record of credit history.
- **Asset finance,** sometimes called leasing, or hire-purchase, or lease-purchase, is debt secured against a specific fixed asset such as a new machine or vehicle. It is often easier to raise than a term loan, and does not require collateral beyond the asset being acquired. It often comes from a finance house rather than a bank, so does not preclude further borrowing from the bank. However, asset finance is often more expensive than bank debt, a track record may be required, and it is usually dependent on a strong expectation of positive cash flow.
- **Factoring and invoice discounting** means that you transfer your accounts receivable or invoices to a factoring company or an invoice discounter, who will pay you in advance (less a percentage to cover their costs and profits) and take responsibility for collecting the payments on your behalf**.** This gives additional working capital, but it can be expensive and it may not be available in every locality. Depending on the arrangement you negotiate, you could be hit with unexpected debt if your customers fail to pay.
- **Supplier credit** is a type of debt achieved by agreeing to delay payments to suppliers. It is usually cheap short-term credit, but not all suppliers will be willing to provide it, and it can be difficult to manage if the timing of customer payments is unreliable.

Lending cover: an example

Lending cover is the ratio of net profit to interest:

$$\text{Lending cover} = \frac{\text{Net profit}}{\text{Interest}}$$

Imagine that your business is forecast to make a net annual profit of $50,000 and that it will pay $10,000 in interest.

$$\text{Lending cover} = \frac{50{,}000}{10{,}000}$$

So your lending cover is 5 and will almost certainly be acceptable to an investor.

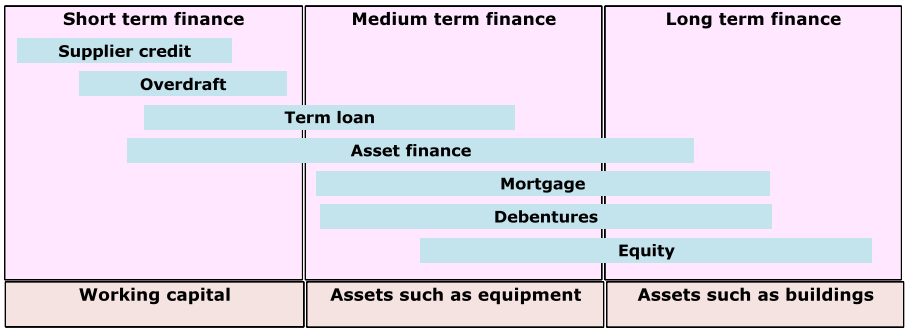
Advantages for the enterprise	Disadvantages for the enterprise
Debt is usually easier to arrange than equity financing, particularly if you have a track record or you are able to provide collateral. With debt, you will retain complete control and ownership of the enterprise.	Debt can be hard to obtain if you don't have a track record or collateral, for example if your organisation is transitioning from a not-for-profit model that does not have a trading history. Repayment schedules are typically quite inflexible, so if revenue growth does not meet expectations then an enterprise can end up with a burden of repayments that it cannot meet. For start-up enterprises, debt may not cover financial needs within reasonable gearing or lending cover limits.

3.6 How do I match investment to my needs?

It is desirable, if possible, to match the length of the funding to the life of the asset. So, investment can generally be divided into three categories:

- Short term: trade creditors and overdraft.
- Medium term: loans of less than seven years, leasing and hire purchase.
- Long term: loans of more than seven years and equity.

Figure 1: Matching finance to need



If you are lucky, you may be able to raise all your finance needs from a single source, particularly if that source is a social investor. Most enterprises find that they need to 'package' support from a number of sources. Investors rather like this because they feel that they are not alone in taking the risk, but it does require more effort from the enterprise. If you have not raised finance before, then it might be sensible to find an adviser with experience of doing this.

3.7 How do I fund fixed assets?

Tangible fixed assets, that is, premises and equipment, are usually defined by their life and divided into medium and long term and are usually funded by equity or term loans. The term of the loan will need to be less than the expected life of the asset. Securing a longer loan will almost certainly depend on the age of the enterprise, and on your track record with the lender. A more established enterprise will find it easier to secure a longer term loan.

Bear in mind that it is often possible to buy equipment on hire purchase, lease or lease purchase (see "asset finance" above). Lease companies will

not have the same concerns about gearing as the banks. They will, however, be interested in your cash flow and whether you can afford the repayments. The equipment will generally remain the property of the leasing company until the end of the lease. You have the legal right to use the equipment for the period of the lease assuming, provided that the lease payments are up to date. At the end of the lease, the equipment reverts to the leasing company, although it is often possible to buy the equipment for a small sum.

3.8 How do I fund working capital

Unless there is sufficient equity in the enterprise (whether introduced as capital invested or as retained profit), working capital is generally funded by supplier credit and an overdraft facility. You may have to pay an arrangement fee for your overdraft, but you will only pay interest on the outstanding balance. Whilst the interest rate for an overdraft may be higher than for a term loan the overall cost may be lower, because the amount of debt outstanding varies.

3.9 Are there typical investment patterns over the life of a growing enterprise?

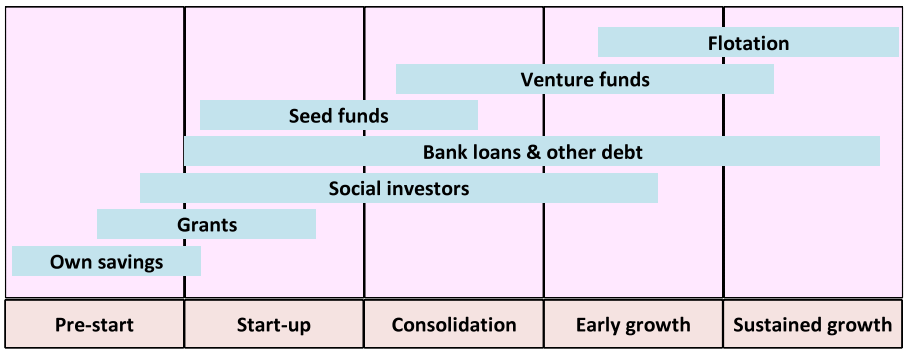
No two enterprises are the same, but there are typical investment patterns, as shown in the figure. Enterprises tend to start with money from friends and family, perhaps backed up by a small bank loan.

> ***"My view is that young companies should be thinking about grants and equity first, then debt. There is so much business risk that they need flexible capital at least for the first few years."***
>
> Rajan Kundra, Acumen Fund

Sustainable energy enterprises may find that they can access grants and social investments that might not be available to enterprises in other sectors. As they grow, they will find it easier to raise debt from banks and others, though generally this has to be matched with finance from elsewhere. Commercial seed funds and venture capital funds typically provide equity investment at a relatively early stage in the growth of a company and they might be persuaded to invest. Not every enterprise goes through every step.

The most successful enterprises may ultimately float on the stock market and become a publicly owned company.

Figure 2: Stages of growth



4. Raising investment finance

4.1 Can I attract investment?

Attracting investment requires that you can demonstrate to investors that you are 'investment ready'. They will look for evidence that:

- you have a clearly defined and potentially profitable market and, ideally, that you are already selling into that market (demonstrated through a good business plan)
- you have a suitable product and, ideally, that you own the intellectual property rights[5]
- you have a committed, professional and experienced management team
- there is an exit strategy[6] for the investor.

4.2 Are there any down-sides from taking investment?

The biggest disadvantage of equity investment is that you may lose some control over the enterprise. However in the long run you are likely to learn a lot from the external investors. If you are able eventually to buy out the investors, then you will secure total control once again.

Depending on the nature of the investment, it can be quite expensive and will bring new financial risks, so care is needed with your business planning and financial forecasting.

For NGOs used to working with grants, it may come as a shock to think in a different way and to expect to repay the investors.

4.3 I think that investment is right for me, what do I do next?

The first step is to agree that investment is required and to agree whether certain types of investment should be ruled out. Depending on the legal format and structure of the business, this may require agreement from the board and, if there is one, the board of a parent company as well. If there are existing investors, they may also need to be consulted.

The next step is to prepare a financial forecast and consider the level of investment required. If this looks sensible, it will be necessary then to prepare a detailed business plan and to share it with potential investors.

If the plan is persuasive enough, investors will then want to visit the enterprise. This is your chance to convince them that what you have on offer is irresistible. If you are looking for a loan, then usually the lender will make an offer on a 'take it or leave it' basis. If you are looking for equity, there is much more scope for negotiation.

One other issue is the level of development that an investor will be looking for – many will prefer to invest in an enterprise that is already operating (even at a small scale) and will be wary of investing in a "plan". This will depend on the investor and you will need to find this out at an early stage.

> ***"Your business plan can also be a useful tool for managing your business and guiding your staff – provided that it is periodically updated to reflect changes that arise as you implement the plan."***
>
> Hari Natarajan, GVEP International (Asia office)

Once you have convinced an equity investor, they will generally make an offer. You may then choose to negotiate. Once you reach agreement, more likely than not, the investors will want to undertake a detailed evaluation process known as "due diligence" before finalising a deal. Due diligence basically refers to the assessment process that the investor will use to assess the suitability of your enterprise. More details are in section 4.13 below.

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[5] Intellectual property rights or IPR are the legal property rights that can apply to an invention or a particular business model – for example a trademark, copyright or patent. For more information: http://en.wikipedia.org/wiki/Intellectual_property_rights

[6] The term "exit strategy" is used to cover the mechanism by which an investor will get their money back, along with any profit.

4.4 Do I need to write a business plan?

Yes, you will need a business plan. This has to provide the potential investor will everything they need to assess whether to risk money in your enterprise. Think of it as a marketing document – you are aiming to 'sell' your enterprise to investors.

4.5 How do I calculate the value of my enterprise or investment?

P/E ratio: an example

The price/ earnings ratio, as applied to small businesses, is the ratio of the value of the business to the earnings (that is, the net profit)

$$\text{P/E ratio} = \frac{\text{Value}}{\text{Net profit}}$$

Usually, you start from the P/E ratio, to calculate the value. If the P/E is three and your net profit is $50,000, then the value of the business is $150,000.

If you are only looking for debt or quasi-equity financing, there is no need to value your enterprise because investors will make a decision based on your balance sheet and your business plan.

However, if you are looking for equity financing, then you need some idea of the value of your enterprise (as well as the amount of money that you need), so that you can negotiate with the investors. This can be complicated for sustainable energy enterprises where a key component of the founders' equity may be the intellectual property for the technology, and the previous investments that have been made in technology development. The valuation of these elements is likely to be agreed in negotiation with the investors.

Investors will value a business or investment based on the price/ earnings (P/E) ratio, that is, the ratio of the value of the business to the net profit (usually averaged over a three year period, to include last year, the current year and next year). Investors will expect to come in when the P/E ratio is relatively low, say three, and exit when it is somewhat higher, say five.

4.6 How do investors get their return?

Lenders get their return through the interest that you pay on the loan, and sometimes through an arrangement fee. Obviously they expect their capital back as well!

Internal Rate of Return (IRR)

It can be helpful to think of the IRR as the compound annual return achieved on an investment. For the mathematically minded, the IRR is the discount rate that generates a zero net present value for a series of future cash flows.

Calculating the IRR can be a little time consuming but there are easy formulae in Microsoft Excel and other programmes that can do it for you.

Equity investors expect to get a return in two ways: firstly through a dividend on their shares and secondly through selling their shares at a profit when they exit, as in the example above. The total return achieved is known as the internal rate of return (IRR). The level required to be "attractive" will vary depending on the investor – from less than 10% up to more than 40%. If you want to learn more about IRR, a good starting place is the UNFCCC guidelbook on preparing and presenting proposals listed in the further information section below.

There are generally three ways in which external equity investors exit – through a buy back by the company (or the other shareholders), through a trade sale (where the company is sold to another company) or through a flotation on the stock market. The most likely route for energy enterprises is through the buy-back – so it is important from the outset to be clear what the investor is likely to be looking for, whether a future buy-back is included as part of the deal you sign, and whether you can afford it.

If the investment is some sort of debt or quasi-equity financing then the exit cost will be far clearer – and again, you should be able to forecast whether you can afford this. Even if you are unable to forecast the likelihood of repaying the investor, they will be looking at this very carefully, and are unlikely to invest if they do not expect to get their return.

4.7 Can I own an equity share if I am not putting cash into the company myself?

Yes! You cannot simply give yourself shares in a company if there are other investors. But all the shareholders together might agree to reward you for previous work by a free issue of shares, or you might be given shares in exchange for intellectual property that you have introduced into the company, or you may take part of your remuneration as shares (or share options).

4.8 What about giving my employees a share in the company?

Many enterprises believe that giving staff a stake in the company increases their motivation and commitment. This does not necessarily require that staff all have shares, though that is a very good way of giving staff a stake. It is possible to design bonus schemes to align staff interests with those of other stakeholders and particularly with those of the investors. If the enterprise is a subsidiary of a not for profit, careful thought will be needed as share ownership schemes or bonus schemes may cause tension between staff working in the subsidiary and in the parent.

4.9 If I want to sell equity, how much should I sell?

This is a tricky one. You need to sell a sufficiently high percentage for the external investors to think that they will get a decent return, but a sufficiently small percentage that you will be rewarded for your efforts and will not lose ownership of the company (which would happen if you sold more than 50%).

It all comes down to negotiation with the investors. Ideally, you should hook an investor first, and then start negotiating on the percentage. If you start by offering too low a percentage to an investor, the chances are that they will not even look seriously at your proposition. The large variety of investment options described earlier also mean that there is considerable scope to design an investment package on which everyone can agree, perhaps with a relatively small percentage of ordinary shares and a high level of preference shares, or perhaps through a quasi-equity arrangement.

4.10 What is the best way to approach an investor? Should I approach more than one?

Yes! Approach more than one. The first approach should generally be the one page summary of your business plan. Once you get to the point of serious discussions, however, it is probably more sensible only to be negotiating with one investor at a time. Most investors talk to each other, and they will not take kindly to competing for your business. Sometimes, you will find that a group of investors want to make their investment as a syndicate, but usually one investor will then take the lead.

4.11 Is it a good idea to have more than one investor?

Sometimes, it is necessary to have more than one investor simply because individual investors do not want to assume all of the risk themselves. From your point of view, however, and the need to manage your investors, you will not want more than two or three. You may also find that some investors would like to have an exclusive relationship with you.

4.12 What about the legal side - who prepares the investment contracts and how do I know if they are fair?

For debt, you will normally have to sign the standard contract provided by the lender. For equity deals, the investor is likely to seek agreement to a considerable number of legally binding requirements. Often, they will wish to amend the articles of the company, so that under certain circumstances,

they can assume control in order to protect their money. Providers of quasi-equity are likely to be far less demanding.

You will need to read everything very carefully. In addition, you should appoint your own legal adviser, with commercial experience, so that you can get independent advice.

4.13 What do investors care about?

> ***"The organisations and individuals that want to invest in sustainable energy all have different objectives – it can be frustrating to try and meet all their different demands. My tip is to make sure you answer their emails in good time, keep a written record of your investor conversations, and don't be afraid to ask them for feedback on what you need to do to meet their investment criteria."***
>
> Ben Dixon, The Ashden Awards

For most mainstream investors, the most important thing to them is making a financial return. However, if the competitive edge of your enterprise derives from environmental or social benefits, then clearly you need to stress those as that will be of interest to the investor.

For "social impact investors", for example charitable foundations that are making investments, the financial return may be less important. They will want to know more about the environmental or social benefits. But you still need to be able to convince them that you have a viable and sustainable enterprise, so that they eventually get their money back.

It makes sense therefore to aim to cover both of these aspects and not to prepare two different plans. If investors are more interested in one aspect than another, then they can ask for additional information.

4.14 How do I make decisions about investment in my organisation?

The ultimate decision on investment will depend on the ownership structure of the organisation. For a not for profit, generally it will be the board who will decide, though you may have members and they may have a constitutional right to have a say. If you are setting up a subsidiary, and the investment is in the subsidiary, then it is far easier for the board of the parent to take the decision, though if the investment comes as debt, and if the parent is asked to provide a guarantee, this may need a members' resolution rather than just a board resolution.

4.15 Do I need to worry about exchange risk?

If you are successful in attracting a foreign investor, it will be important to agree on the currency in which the investment will be made. If the investment is not in your currency, then you are taking an exchange rate risk. It may be possible to 'hedge' the risk, for example by putting some of your cash reserves into an account in the same currency as the investment. It may be possible to persuade the investor to take the risk.

5. Business planning

5.1 How should I present my business plan?

The ideal business plan will be no more than 10 pages long, together perhaps with some appendices. Considerable guidance on writing business plans is available (see further information below) and the appendix to this guide provides a detailed overview of the content of a business plan.

In addition to the business plan, you should write a one page summary which you would initially send to investors, only sending the full plan if they ask for it. However, you cannot write the summary until you have completed the full plan.

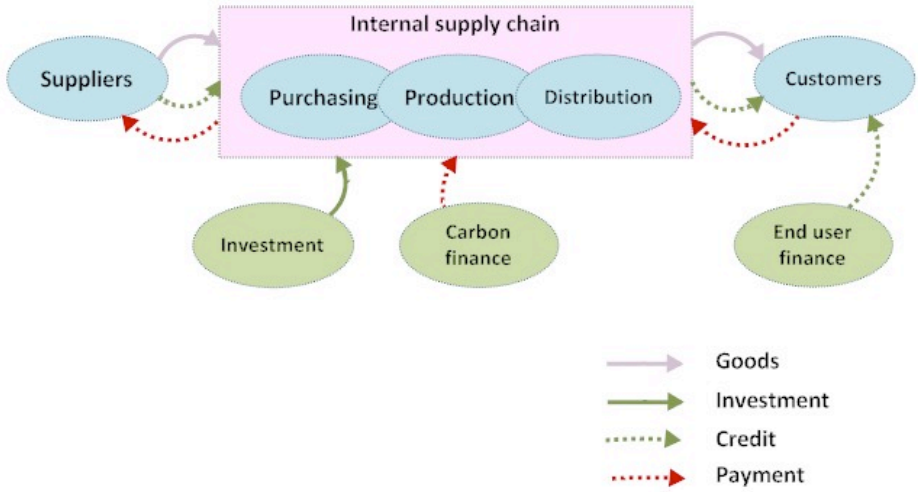
You should pay particular attention to explaining your marketing and may need to include a section on carbon finance.

5.2 How does my enterprise relate to customers and suppliers?

It is important to understand your customers clearly, and to be able to describe them accurately in your business plan. This will help you to market your product or service – and it will help you when you are talking to investors. It will also help you to think about your suppliers – and what you might need to do to ensure reliability of supply. The way that customers, enterprises and suppliers link together is known as a supply chain.

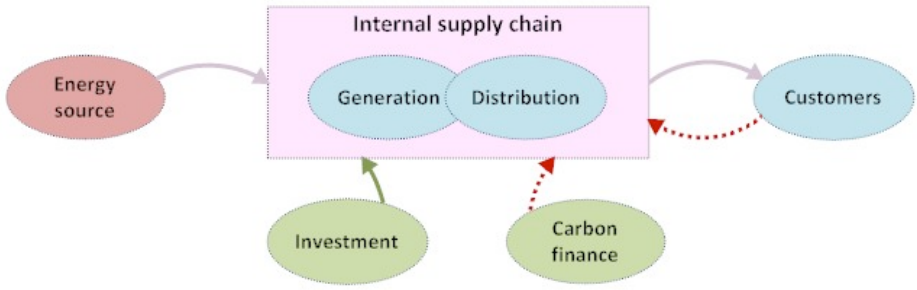
All enterprises fit into supply chains. Some of the links in the chain may be internal whilst others will be external. Understanding where you fit, particularly where there are many external links, will help you better serve your customers. It will also help when describing your enterprise to investors. A simple supply chain for a product-based sustainable energy enterprise (e.g. a solar lantern company) is shown in figure 3. This might apply to a manufacturer but could equally apply to an installer or a retailer. The enterprise buys materials or finished goods from a supplier; maybe it assembles or manufactures thus adding value; it then sells to customers. There may be scope to reduce the cost to consumers or increase income to the enterprise by attracting carbon finance. If the capital cost is high, consumers may need assistance with finance, which may be a barrier to sales unless you can help.

Figure 3: Product based supply chain



If you are generating energy and selling it to customers (Fig 4), then once you have constructed your generating facility, the major input will be your energy source (e.g. flowing water for micro-hydro). Your internal supply chain will typically cover the generation process and the distribution to customers. You operate as an energy service company or a small utility company and your customers will pay in regular instalments. As in the earlier example, there may be the opportunity for you to attract carbon finance. Unless you decide to charge up-front connection fees to your customers, they are unlikely to need end-user finance.

Figure 4: Service based (generation) supply chain



5.3 How do I include carbon finance in my business plan?

Businesses that produce carbon savings may be able to benefit by selling the savings as carbon credits. This is a way of generating additional income for the business. It is critical that carbon finance is addressed early in the business planning process – as it can take a very long time. It is a good idea to consult with a specialist advisor. Some summary details are given below – for more information please see the parallel guide being prepared by GVEP International.

> ***"Beware - carbon finance is highly touted as a source of finance, but it is still mostly a pipe dream in Africa. It is not a core source of investment finance where I am working."***
>
> Daniel Macharia, GVEP International (East Africa office)

Most sustainable energy enterprises will be reducing emissions of carbon dioxide and other greenhouse gases. This is because their customers switch from higher carbon energy sources (e.g. kerosene lanterns) to lower carbon energy sources (e.g. solar home systems), or because they switch to more efficient ways of burning biomass (e.g. with improved cooking stoves). If so, the enterprise may be able to market the carbon savings as carbon credits in the global carbon markets.

There are two primary markets.

- In the larger "compliance market", enterprises, governments and others buy carbon credits (known as Certified Emission Reductions or CERs) in order to comply with legal caps on the total amount of CO_2 that they are allowed to emit.
- In the smaller "voluntary market", individuals, enterprises or governments purchase carbon credits (known as Verified Emission Reductions or VERs) to offset against their own carbon emissions.

Converting carbon savings into carbon credits that can be sold in the carbon markets involves detailed registration and verification processes, and the cost and time required for these processes should be carefully assessed to make sure that it is worthwhile, and included in your business plan.

The other key consideration is additionality. In order to qualify, the revenue from carbon finance must be essential for overcoming a barrier (financial, technological, or institutional) that would otherwise prevent sale of the product or service. For example, it may be used to reduce the price of the product or service and so make it affordable to your customers. If there is no barrier and the sales would happen without carbon finance, you are not eligible for carbon credits.

If you are seeking carbon finance, your business plan needs to be clear about additionality, for example by showing evidence for the how carbon finance will reduce the price of products compared to competitors.

Incorporating basic carbon benefit information in a proposal will also serve to demonstrate a significant environmental impact to a social impact investor.

6. Finding investors

6.1 What kind of investors are out there?

There are a wide range of potential investors, including

- International investment funds
- International charitable funders (including donors and grant giving trusts and foundations)
- International challenge funds (such as the African Enterprise Challenge Fund)
- Carbon funds
- Local investment funds
- Local charitable funds
- Local lenders, including banks and micro-finance

6.2 Should I look for local or international investors?

This is a difficult question to answer. There are a growing number of international investors but the demands for their support are growing even faster. On the other hand, they may have much more experience of investing in your sort of enterprise, so you may get a quicker answer. Local investors are close to the action and may be a longer term prospect once international investors have moved on. You may also find that the legal context in your country favours local or international investors. The real answer to the question is that you should look for both.

6.3 How do I find potential investors?

> ***"Early stage investors really drive the direction of a young company. Ideally, you will find investors with common values that will add strategic value, create networks and can bring technical expertise to the table. It really is about more than just the money."***
>
> Rajan Kundra, Acumen Fund

Scour the internet. There are some investor directories suggested in the next section. Talk to other enterprises in the same field, even if they are in a different country. Talk to your local bank and business adviser, if you have one, as they are often good sources of this sort of information. Chambers of Commerce and Trade are usually well connected and should be able to give you a list of investors.

Young companies need advisors – for example from technical and financial areas (including carbon finance) and universities. These networks are also often where investors are found.

7. After investment

7.1 How should I involve my investors after the investment has been agreed?

If you have succeeded in attracting equity, it is quite possible that the investor will require a seat on your board, and so will require exactly the same information provided to all the other directors. Similarly a bank may ask for quarterly or even monthly management accounts.

Even if none of your investors requires any reporting, however, it is sensible to keep them in touch with your progress. You should be preparing monthly management accounts in order to manage the enterprise effectively. I would suggest however that you send management accounts with a short update to all of your investors every quarter. Tell them how you are doing, whether you are on target, and of any corrective action that you plan to undertake if you are slipping behind target.

This will not only demonstrate that you are being professional in your management of the enterprise, but will also reassure the investors that you are in control. It will make it more likely that they will support you if you discover that you need a bit more investment in the future.

7.2 What should I do if things change and the plan does not progress as we hoped?

If things go really badly, then tell the investors at an early stage. They may be able to help you turn it round – after all, they don't want you to fail any more than you do.

8. Further information

8.1 Preparing business plans

There is a wide range of sources of further information which can assist you to research the market, assess the opportunities and prepare a business plan. Here are a few:

- "United Nations Framework Convention on Climate Change - Preparing and presenting proposals: A guidebook on preparing technology transfer projects for financing". This is essentially a guide to business planning though does include descriptions of types of investment, explains what different investors look for and the necessary steps to secure

investment. It has a large number of worked examples and some good templates. See www.eandco.net/tagfiles/2/Practitioners_Guide_0e87081d.pdf

- "United Nations Environmental Programme - Rural Energy Enterprise Development Toolkit: A Handbook for Energy Entrepreneurs". This is a step-by-step guide to developing a business plan to attract financing. See www.areed.org/training/toolkit/Doc_new/REEDToolkit1-4_web.pdf
- GREENTIE (see www.greentie.org/finance/index.php) has fairly basic information on becoming investment-ready and seeking investment finance.
- The World Bank has a Carbon Finance website which has links to carbon funds and facilities and provides advice on seeking carbon finance: http://go.worldbank.org/9IGUMTMED0

8.2 Sources of finance for sustainable energy enterprises

And there are many sources of finance. Here are a few:

- Global Village Energy Partnership International offers partners access to sources of funding, provides best practice guides and other information, and can put you in touch with other projects similar to yours so that you can share your knowledge and experiences and learn from others. See www.gvepinernational.org.
- The Sustainable Energy Finance Initiative has a directory of lenders and investors who actively provide finance to the sustainable energy sector worldwide, though it is largely restricted to investors from developed countries and to multi-lateral donors. See www.sef-directory.net.
- E+Co invests through both debt and equity in local energy enterprises that make a positive social and environmental impact and generate financial returns in Africa, Asia and Latin America. Investments typically range from US$25,000 to US$1m. It backs up its investments with tools and know-how to make clean energy enterprises successful. See www.eandco.net.
- GroFin, based in South Africa, but working in 9 countries in Africa and the Middle East is a specialist SME finance and development company offering an innovative combination of risk capital and business development assistance. It invests responsibly in viable businesses, providing unique solutions for each client, providing financial support, and additionally sharing skills and transferring business knowledge. This combination of money and mentoring assists entrepreneurs to work profitability and encourages sustainability and success. GroFin supports SMEs through all stages of business development, from start-up, through growth to expansions. See www.grofin.com
- Acumen Fund is a non-profit venture capital fund, focused on supporting the delivery of critical services – water, health, housing, energy – at affordable prices to businesses in India, Pakistan, east Africa and south Africa. Acumen Fund aims to show that small amounts of philanthropic capital, combined with large doses of business acumen, can build thriving enterprises that serve vast numbers of the poor. See www.acumenfund.org
- Carbon Finance Africa aims to facilitate and stimulate the carbon sector in Africa, through an innovative matchmaking facility which assists project developers in finding financial partners and their counterparts in sourcing carbon projects in Africa. Currently the focus is on South Africa though there are plans to expand further afield. Their website includes general information on climate change and carbon finance as well as country-specific information on the investment climate and carbon finance in South Africa. See www.carbonfinanceafrica.org.za

- ERM Foundation Low Carbon Enterprise Fund invests in small businesses in the developing world where the products or activities help combat climate change. As the not-for-profit Foundation of ERM (the global consultancy) their goal is to support those businesses that would otherwise struggle to get funding and where there are clear, additional social benefits. See http://www.erm.com/erm/foundation.nsf/pages/foundation

9. Conclusion

It can feel daunting setting out on a new venture – especially when you have to raise all the finance and make enough profit to reward the investors not to mention paying the staff and serving the clients. It will require hard work and long hours; it will need commitment and tenacity. But it can also be immensely rewarding to know that you are making a real difference. And you are not alone – there is considerable support available and many people who are willing to give advice and assistance to help you turn your dream into reality – for you and all the people who will benefit from your service.

Good luck!

10. Acknowledgements

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- Rajan Kundra, Acumen Fund
- Svati Bhogle, TIDE

Appendix 1: Business plan outline

A1.1 Introduction

A business plan helps you to define the purpose of your enterprise and your vision for where you want to be in the future; it describes your goals and targets and explains how you are going to achieve them. It is basically an outline of how your enterprise will operate, as well as a guide to measure its progress. You may want to differentiate between 'planning', a continuous activity, and 'writing a business plan' which you may only do once a year or when you are seeking external finance. The annual plan may just have a few marketing objectives and a financial forecast; a plan to raise finance will need to be more comprehensive, though should be no more than 8-10 pages. This guide covers all the key areas that should be addressed in your plan. Treat it as a guide, not as a straightjacket. You may need to present information in a different order; you may not feel that you need every section; you may need other sections. But when you have finished, do use this a crib sheet so that you don't forget anything.

A1.2 Why do you need a business plan?

A good business plan can help you to:

- Clearly identify and communicate your business idea and the reason for it;
- Bring together your ideas and research into a readily understandable format;
- Identify any further research that is required;
- Set your business objectives and performance targets; and
- Monitor your business' performance.

A1.3 What should your plan include?

Your plan should provide evidence that your enterprise has the potential to be a success. It should contain:

- A description of what your enterprise will do;
- Details about your enterprise's aims and objectives;
- Details about the products and/or services your enterprise will provide;
- Details about your target customers and the trends affecting your target market;
- An assessment of your competitors' strengths and weaknesses;
- An explanation of how your enterprise is different from the competition, that is, your competitive edge;
- Details of how you intend to market your product or service;
- How and where the enterprise will operate; and
- Financial requirements.

A1.4 Cover sheet

Serves as the title page of your business plan. It should include your company name, address, phone number, contact person and date of preparation. Remember that your business plan is part of your marketing, so ensure that it is prepared with the same professionalism and eye for detail that you would expect to use in other aspects of your marketing.

A1.5 Executive Summary

If you keep your plan short, then this probably does not need to be more than a couple of paragraphs. It should include

- The enterprise's purpose and objectives;
- A description of the enterprise;
- A description of objectives and why you need investment;
- An explanation of how much you need and the form in which you would like it (equity, debt);
- The reasons why you think you will be successful;
- Social and environmental benefits;
- How and when the investors will get their money back and, for equity investors, their expected IRR.

A1.6 Enterprise description

What does the enterprise actually do? Give a concise description of the enterprise, and its purpose, in a way that anyone reading it will understand what it is that you want to do.

A1.7 Goals and objectives

What are your plans for the enterprise and what do you want it to achieve? Think about where you want to be in three or five years' time, and what you will need to do to get to that point. For example, do you want your enterprise to:

- Be recognised for your innovative new ideas?
- Grow quickly?
- Be a local specialist?
- Be well-known locally for high-quality, premium products/service?

A1.8 Social and environmental benefits

You should explain the social and environmental benefits that will be achieved if your enterprise is successful.

A1.9 Target market (current and future)

You need to understand the market and know to whom you plan to sell. How will you fit into the market? Which specific market opportunities or gaps you will exploit? You should look at:

- Market trends;
- Purchaser demographics;
- What influences the market;
- Major competitors and other products already available in the market.

Think carefully about the customers you want to attract and define their characteristics. Investigate how many potential purchasers fall into your target group and undertake some market research.

If your customers are other enterprises, rather than domestic consumers, describe where you fit in the value chain.

A1.10 Analysis of competitors

You should look at other enterprises that will be in direct and indirect competition with you. You should analyse their products, customers, market share, marketing strategy, growth and facilities.

A1.11 Sales and marketing plan

Now that you have defined and described your target market and customers, you need a marketing plan describing how you will reach them and sell to them. It should cover:

- Price, including an explanation of whether you are aiming to differentiate your product or are aiming for cost leadership (bearing in mind that most small enterprises simply do not have the economies of scale to achieve cost leadership);
- Place, that is, how you will distribute your product or service
- Promotion, that is, the marketing method(s) you will use to reach your target customers;
- A timescale or timetable for each marketing activity;
- How much your marketing will cost you, and what resources you will need;
- How you will monitor and review your marketing progress;
- How you will handle the response to your marketing efforts;
- The risks you will face.

A1.12 Sales targets

Set out some targets you intend to achieve. These should be broken down month-by-month, and could include goals such as:

- Sales of different product types by volume and value;
- Sales from different customer groups;
- Sales from different distribution methods (for example delivery to customers or customer pick-ups).

A1.13 Operational requirements and costs

Work out what equipment and services you will need to run your enterprise and estimate how much they will cost. Outline your requirements for things like:

- Location/premises: Will you rent? What facilities will you need? What will your premises cost?
- Equipment: what equipment is needed and what will it cost. Will you buy new or second-hand, hire or borrow?
- Staff: Do you need to take on staff? Will you need to train them first? Will you employ more people in the future?
- Suppliers: Have you found suitable suppliers? What are the benefits of using the supplier(s) you have chosen? Have you considered what would happen if your main supplier failed?
- Licences: Do you need any trading licences before starting your enterprise? If you do need a licence, do you know where to get it from, when you need to apply for it and how much it will cost?

A1.14 Financial statements

If you are already in business, you will need to provide copies of your profit and loss account and balance sheet for up to the last three years. Put summary figures in the plan and detailed figures in an appendix. In addition, you will need to provide financial forecasts – monthly operating budget, cash flow forecasts, forecast profit & loss accounts and forecast balance sheets – for the next two or three years, and probably up to five years if you are looking for equity investors. Put summary figures, perhaps annual, in the plan and detailed figures in an appendix.

Explain how you have calculated costs and prices and show the breakeven point. Look at the sensitivity to changes – sudden increases in costs or sudden loss of sales; prepare a risk analysis and explain the actions to mitigate the risks.

Explain what finance is already available to invest in the enterprise and how much extra is needed. Explain how the investor will get their money back and, in the case of an equity investor, what return they might expect.

You will probably want to provide two scenarios, one without carbon finance and one with, so that you can demonstrate how much more successful the enterprise might be with carbon finance.

A1.15 Financial management

You should explain the procedures that you have to ensure that you retain control of your enterprise financially.

A1.16 Appendices

Use the appendices to provide evidence to back up the assertions and statements made in the main parts of your business plan. Those most commonly included are as follows:

- Brief resumes of key staff – limited to one page, including: work history educational background, professional affiliations, honors and special skills;
- Market research – detailed results of any market research that you may have undertaken;
- Detailed financial statements – most likely you will just have a summary of accounts and financial forecasts in the main body of the plan, so put the more detailed figures in an appendix;
- Letters of reference – letters recommending you as being a reputable and reliable enterprise worthy of being considered a good risk;
- Legal documents – papers pertaining to your legal structure, proprietary rights, insurance titles etc;
- Miscellaneous documents – other documents that have been referred to but are not included in the main body of the plan (e.g. location plans, demographics advertising plan, etc.).

Appendix 2: Glossary

Assets Goods, resources and property belonging to the enterprise.

Balance sheet A statement showing the assets and liabilities of an enterprise at any particular moment in time.

Breakeven point The breakeven point is the point at which the income from sales exactly equals all the costs of the business.

Capital employed The total of equity and debt, that is, all the capital used by the business.

Contribution The amount contributed by a sale is the income generated by that sale less the direct cost of producing that product.

Creditors Those to whom money is owed for goods, cash, services, etc.

Current assets Assets in a cash or near cash state (e.g. cash, debtors, stock).

Debt Money which has been borrowed to finance the enterprise.

Debtors Those who owe you money for goods, cash or services supplied.

Depreciation The amount charged to the profit and loss account each year to represent the wear and tear of machinery, equipment or industrial buildings.

Dividend A payment made from profit after tax to the owners of an enterprise.

Equity The equity in an enterprise is the (shareholders') capital introduced by the owners, together with any retained earnings.

Gearing A measure of debt as a proportion of total finance (i.e. ratio of debt/debt plus equity).

Internal rate of return The percentage annual return achieved on an investment, sometimes known as the yield

Interest cover (also known as lending cover) A measure of the ease with which an enterprise can meet its interest requirements. The interest cover is the net profit before interest and tax divided by the interest payable for the same period. Lenders tend to look at this figure!

Net profit The actual profit made by the enterprise after the deduction of all expenses. Remember that if you are self-employed, your drawings are not regarded as an expense, whereas wages for your staff, and you if you are director of a company, are expenses. Tax is not regarded as an expense.

Profit and loss account A summary of all the income and expenditure for the accounting period.

Profitability A series of measures which show how profitable an enterprise is. These include gross profit and net profit. Probably the best measure is "profit before interest and tax", ie the sales income less all the direct costs and all the overhead costs except interest. The profit margin is PBIT/sales.

Reserves Profits retained within the enterprise.

Revenue The income generated by the enterprise for a specific period.

Security (also known as collateral) Assets, whether owned by the enterprise or by individuals, which are pledged to the bank and which may be seized by the bank in the event that you fail to repay the loan for which security has been pledged

Solvency A measure of a enterprise's ability to pay its bills as they fall due. If it cannot, then it is insolvent.

Stock Goods held for sale in the ordinary course of business.

Turnover Net sales, income that is, total sales less allowances.