

*Ernst & Young Entrepreneurial Services*



*Guide to producing a*  
**Business Plan**

 **ERNST & YOUNG**

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## Business Planning

Producing a business plan offers an excellent opportunity to consider all the facets of a business or a project, testing feasibility and providing greater confidence in decision-making. It will also identify future financing needs and is usually a necessary step in raising external finance.

It stems from the strategic planning process which is the evaluation of a business's competitive advantage and opportunities. The business plan will develop in more detail the broad action points derived from your strategic planning, establishing corporate goals, setting objectives, evaluating the operating environment and producing ways to measure their successful achievement.

A business plan can be a useful ongoing tool, as it can be used to measure progress as well as to communicate between management, staff and existing investors/bankers. To achieve this it must be kept up to date as the business moves through different stages, from start-up to rapid growth and maturity. A company's strategy must also change along with its objectives.

This brochure focuses on the necessary steps to produce a business plan for the purposes of raising finance, giving guidance on what to include in, and how to present, the plan. It also incorporates tips which are derived from Ernst & Young's substantial experience in assisting a wide range of clients to produce business plans for many different reasons.

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# Preparing a Business Plan

## 1 GETTING STARTED

Guidance on writing the plan depends on the main objective of it. We answer the most common questions raised on writing business plans below, but the underlying rule is **WRITE FOR YOUR READER**. This means both writing in language that the reader will understand, and covering the issues that the reader will want to know about.

### **E&Y TIP**

Some 85% of plans are not seriously considered by investors so if the purpose of the plan is to raise finance, it is vital to identify the likely sources of finance at an early stage in order to **WRITE FOR YOUR READER**.

### ***Identify your objectives***

Identify the reasons for writing your plan, and identify your target audience. Consider what your target audience already knows about your business, what else they will want to know and how they will use the information given.

You should also consider whether there are any potential conflicts between what they will want to know and what you want them to know. These potential conflicts need to be considered and resolved before you write the plan.

## 2 DRAFTING THE PLAN

### ***Who should write the business plan?***

A business plan reflects your thoughts and plans for your business, and as such must be written by **YOU**. You may need some help from advisers in challenging your comments and assumptions, deciding on content and overall format, and you may also need assistance in preparing financial projections.

### ***What should the plan cover?***

Any plan must include the key areas of the market, management and the financial impact of the plan.

There is no agreed format for all business plans, however they should follow a logical flow in explaining the idea, the benefits and the results. To help with this we have set out in Section 3 a general outline of what should be covered and how the plan should be structured. In some situations only part of this outline may be appropriate, certain sections may be amalgamated or further separated, but in all cases you should tailor the plan to your specific circumstances.

***How long should it be?***

There is no definitive guidelines on the length of your business plan. You should keep it as short as possible whilst covering the subject adequately, and, to achieve this, much of the detailed information can be relegated to appendices.

***How do I maintain flexibility?***

To achieve its objectives, the plan needs to be specific. It may be useful to discuss alternative options and the impact they would have, but the plan should be based on management's current preference.

***How should it be presented?***

Presentation should be entirely aimed at captivating the interest of the reader and ease of reading and understanding. For example, page and paragraph numbers should be used along with cross-referencing, simple graphs and graphics, and colour photographs, if this assists understanding. Binding and covers should be practical and should avoid both amateurish and lavish appearance.

**3 PREPARING FINANCIAL PROJECTIONS**

The plan needs to include projected profit and loss accounts, balance sheets (including an opening balance sheet), cash flows and the underlying assumptions. The assumptions must be supported by, and consistent with, your descriptions and explanations in the rest of the plan, or differences explained.

***How can I forecast future results?***

Forecasting the probable growth pattern and results of a business into the future is a difficult task. However, it is critical to assess the likely impact of the plan on the business's financial condition. The key starting point is the sales forecast, which must be based upon the market and demand rather than production capacity, sales force or service hours available.

It is recognised by financiers that the environment in which a business operates is subject to changing factors and the assumptions underlying projections must therefore similarly be capable of change. Nevertheless, prospective investors will use the projections to gauge whether the investment is capable of meeting their required rate of return, and significant deviations from projections may result in changes in the terms of the finance.

***Should my projections be optimistic?***

It is advisable to aim for the middle road and to be as objective and realistic as possible in compiling financial projections and, particularly, those relating to sales revenue. If in doubt, be conservative and discuss potential "up-sides" in the narrative. The problems of estimating future costs are well recognised and it is acceptable to include a contingency in the projections to cover such uncertainty.

**E&Y TIP**

Test the sensitivity of the projections and assess the financial risk implicit in them by assessing the impact of changes in the key assumptions which are most at risk. Consider your assumptions regarding fixed versus variable costs, and review the impact on your cash requirements.

***Should my projections allow for inflation?***

It is often argued that by ignoring the effect of inflation on both sales revenues and costs there will be no distortion of the financial projections. Whilst it is certainly easier to ignore inflation, this may prove misleading if the prices of certain key items in the projections are expected to be significantly different to the general rate of inflation. Also, where increases are expected to be significant, an understatement of the working capital requirement could arise.

In most cases, therefore, we would advise that effects of projected inflation should be built into the projections.

**4 WRITING THE PLAN*****Produce an outline***

Prepare an outline plan based on the objectives and the readers' requirements identified above. Your outline should incorporate the key points to be made for each heading and sub-heading, and the more detailed you make this, the easier the eventual writing of the plan will be.

Having produced an outline, review it for the necessary level of detail required for each section. Consider the sources of supporting information and whether further research is required.

***Write your plan***

Use the financial projections to ensure that the plan you have in mind is financially viable. Ensure that your detailed assumptions are recorded in order, so they can be justified by explanations in the narrative sections.

The narrative sections should address all the issues identified in your outline, and the assumptions made in producing the forecasts.

***Review your plan***

Review your plan to ensure it adequately addresses key issues, is understandable for the target audience, and that it meets your objectives.

The plan should ideally be reviewed by experienced businessmen or advisers who have some knowledge of the industry and your target audience.

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## Outline Contents and Structure

There is no agreed format for all business plans. However, they should follow a logical flow in explaining the idea, the benefits and the results. We suggest a general outline below, although, as only part of this outline may be necessary in some situations, certain sections may be amalgamated (such as Market Analysis and Marketing and Selling) or further separated (such as Products and Production). In all cases you should tailor the plan to your specific circumstances and audience.

A contents list should be included to assist readers in locating specific sections, which should generally include the following:

Executive Summary	1
Background	2
Products and Production	3
Market Analysis	4
Marketing and Selling	5
The Management Team and Organisation	6
Funding Requirements	7
Financial Projections	8
Key Issues – Risk Assessment and Sensitivity Analysis	9
Action Plan and Milestones	10
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## 1 Executive Summary

This section is important for all plans produced for third parties as it sets the scene, explains the purpose and summarises the whole plan, enabling it to be read efficiently. It is particularly important when raising finance as potential investors receive many business plans and may make an assessment of your business before reading the main body of the plan.

This Executive Summary should summarise the key points of your proposal, including:

- the purpose of the plan
- management's ultimate goal and the company's distinguishing features which will be critical in achieving this goal
- the business opportunity
- the size and type of market the product or service is aimed at
- significant product/service features
- the management team, their experience and how they will realise the opportunity
- critical milestones
- financial highlights, such as turnover, gross profit, earnings before interest and tax and profit or cash flow turnarounds
- funding requirements.

### **E&Y TIP**

If the purpose of your plan is to raise finance, the Executive Summary must attract the investors' interest by highlighting the potential idea and the ability of management to realise that potential.

## 2 Background

This should provide a brief summary of the business and the development of the business idea and the company to date. The summary should explain how the opportunity was identified and its progress to date.

Financial highlights for the last three years should be summarised, where applicable, including the highlights for the year to date. This section should introduce what you consider to be the key result areas, used to monitor your business. The underlying trends should be identified and explained, along with reasons for any exceptionally good or poor performances.



### 3 Products and Production

This section should explain, without technical jargon, your principal products and services, their applications, and distinguishing features. The main purpose of explaining the product is for the reader to understand the market, any unique selling points and, consequently, the business opportunity.

To demonstrate the distinguishing features, the principal markets and market needs should be highlighted, although they should be discussed in further detail in the following section.

*Examples include:*

*“The smaller size and lower weight enables easy and quick aircraft fitting, without affecting flight characteristics.”*

*“The proven efficiency of our production line provides a low cost advantage over our competitors, and the lowest delivery time in the industry, enabling customers to reduce stock levels.”*

*“The size, location and low cost of the premises offers the widest range of service to the widest population, at the lowest cost.”*

*“The attractive appearance of the plants, and their characteristics of frost and damage resistance and rapid spread will particularly appeal to public authorities who have thousands of acres of landscaping to plant and maintain.”*

#### **E&Y TIP**

Be market led. Distinguish your product or service via a tabular comparison with competitors, by key market factors such as price, delivery time, quality, payback period, etc.

A checklist of key questions to be covered in this section is given in Appendix 1.

### 4 Market Analysis

This market analysis section is of critical importance. It must clearly identify your understanding of the market, its characteristics, and your position within it.

Customers and potential customers need to be identified, and factors such as customer needs and decision factors should be fully explained, and supported by third party comments.

The absolute size of your market or niche should be outlined, or estimated by reference to competitor information. Your current and forecast market share need to be included. The use of external reports or research is critical to strengthen the reader’s understanding and belief in the market.

#### **E&Y TIP**

A common mistake is merely to state what profits will result if only a small market share is achieved. Your plan must explain what market share you expect to achieve and how you will achieve it.

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## Outline Contents and Structure continued

Analysis of market segmentation can be one of the most significant parts of the plan and the different characteristics of each segment, including exports, must be clearly explained. Identify your largest existing, and targeted, customers in each segment.

*For example:*

*The plants are ideally suited to the amenities and landscaping market, and the garden plant market. Numerous Councils have expressed interest having seen the plants on trial, and two major suppliers to national garden centres have requested European exclusivity.*

The identity, distinguishing features and expected plans of your major competitors should be given, along with an explanation of any barriers to entry which prevent or hinder new competition.

A checklist of key questions to be covered in this section is given in Appendix 2.

### 5 Marketing and Selling

Having demonstrated that the market exists, you must still go out and win those customers. This section must explain and justify your marketing and selling strategies, including pricing.

#### **E&Y TIP**

Include evidence of customer reaction, interest or references.

*For example:*

*Market research has identified a real need in the Midlands, where there is currently no all round service of the quality and reliability offered by us. Several large customers have already provided letters of intent to use the service.*

You will need to assess your competitors, explain how they are likely to react, and the impact on you and your plan. Your competitors will not simply shut down and watch you progress.

A checklist of key questions to be covered in this section is given in Appendix 3.

### 6 The Management Team and Organisation

By this stage your plan will have demonstrated the potential of your product or service. But at every stage of your business's development, the investor is investing in people, and now you must prove that the management team is able, and likely, to realise that potential, particularly if the aim of the business plan is to raise finance.

You should identify your key members of the management team, explaining why they are key and demonstrating the relevance of their skills, previous achievements and experience to their responsibilities.

**E&Y TIP**

Select management's background and skills that demonstrate that THEY WILL make a success of this business.

*For example:*

*The Sales Director has enjoyed wide experience and success at X Limited and Y Plc, her current employer, where she has been the prime influence in tripling turnover in the last four years. In addition, many of the Sales Director's existing customers have expressed interest in the benefits of our new product.*

It may be useful to provide a current and projected organisation chart, clearly showing responsibility and reporting lines.

**E&Y TIP**

Recognise any important skill gaps or experience limitations in your management team. These can then be addressed up front with investors, often via suitable non-executive directors.

A checklist of key questions to be covered in this section is given in Appendix 4.

**7 Funding Requirements**

The extent of immediate and future funding requirements must be identified, along with the uses to which they will be put. Anticipated sources of funds should also be identified.

The current financial structure should be stated including details of ownership and current shareholdings.

**8 Financial Projections**

The assumptions behind your projections are critical, they require careful thought and must be consistent with the previous narrative. Too much financial information can be worse than too little. Each company must show those figures, the key result areas, that it believes are most important. Detailed financial data may be included in the appendices to the plan.

Projected profit and loss statements, balance sheets and cash flows should be given. Monthly profit and cash flow forecasts should be given for at least the first year and quarterly thereafter if the business is seasonal by nature.

The key assumptions underlying the projections should be given and justified, as well as compared with historic and current achievements.

**E&Y TIP**

Test the data using several different assumptions to determine whether the final information is reasonable.

**9 Key Issues – Risk Assessment and Sensitivity Analysis**

Produce a summary of the critical success factors of the business, along with its key strengths, weaknesses, opportunities and threats, noting how weaknesses and threats will be dealt with.

Any business idea will have risks, and the business plan will have much more credibility if those risks are identified rather than ignored. You should identify the main risks to the business, and show their potential impact on the financial projections.

Explain what you will do to limit the chance of the risks occurring, and how you will minimise their impact if they do occur.

*For example:*

*MBA faces the following potential risks:-*

- 1- Pre-emption by a competitor, as there are significant advantages in being the first to tie in NHS Trust Hospitals to an in-house service.*
- 2- MBA's ability to negotiate favourable contracts with Hospitals.*
- 3- Failure to generate sufficient throughput to achieve optimum running levels.*

*MBA will mitigate these potential risks as follows:-*

- 1- MBA aims for at least fourteen centres by 199X, with detailed discussions already under way. MBA is determined to be the pre-emptive force expanding as quickly as operational efficiencies allow.*
- 2- Contracts with Hospitals will aim to develop a long term, mutually beneficial, relationship. A portfolio of potential sites will be developed with subsequent sites ready to progress quickly if a particular deal falls through.*
- 3- MBA will instigate a proactive marketing campaign, aimed at all stages of the referral process, rather than relying on latent demand. Referring consultants will be tied in via a share ownership scheme.*

**10 Action Plan and Milestones**

List the key stages necessary to achieve the plan, in chronological order with a note of responsibility for completion, and the current status of each stage.

*For example:*

*Complete Quarantine and Agricultural Authority Tests*

USA	September X1	PD
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*Complete Trials*

UK	Completed March X1	
Middle East	Full year commercial trial launched June X1	
USA	March X2	QD

*Appoint Distributors*

UK	Appointed April X1	
Middle East	Trial appointment June X1. Renew X2	QD
USA	May X2	MD

## 11 Appendices or Exhibits (where applicable)

Appendices can be a very effective presentation tool, if they are used to supply important supporting detail which contributes to the reader's understanding and confidence, without being critical to understanding the opportunity.

- Curricula vitae of key managers and employees
- Pictures or sales literature of the product/prototype
- Professional references
- Market research and articles from trade journals
- Patents
- Financial data
  - Detailed projections
  - Historic audited accounts
  - Current management accounts
- Role of Advisers/Engagement letter

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## Raising Finance

One of the main uses of business plans is as an external document to assist in raising finance, which is why we discuss below the most common questions arising from businesses trying to raise finance.

### Who should we send the plan to?

*Whether the document should be sent to a bank or similar lending institution or to a venture capitalist is determined by the level of risk suffered by any investor, the use to which the funds are to be put (and therefore the type of funds sought), and the amount that management wishes to raise.*

*It is important not to flood the Venture Capital market with copies of your plan, and not to waste valuable time by sending it to inappropriate investors.*

### Is venture capital or bank loan finance preferable?

*The decision on the appropriate type of finance depends on a number of factors including the level of projected gearing, the risk attaching to the investment, the projected level of return and cash generation, and the period for which funding is required. There is no hard and fast rule that can be adopted. Each venture and each proposal must be considered on its own merits.*

*It may be possible to arrive at a package of finance, drawing on a number of different sources, which enables the overall cost of finance to be reduced.*

### How should we structure the finance required?

*Management teams often feel obliged to suggest a suitable financial structure for the required finance. In practice most investors will wish to make this judgement themselves so as to meet their required rates of return and other investment criteria. While it is not necessary, therefore, for management to be overly concerned with this aspect, it is advisable that they consider the amount of debt which the venture can bear, subject to cash flow and security considerations, thereby minimising the amount of equity required. Management should also seek professional advice on offers received from financiers.*

### How long will it take to raise finance?

*This depends partly on the nature of the funding proposal – clearly an existing business raising additional debt finance from its current bankers may do so in far less time than a new green field project raising venture capital. Typical time scales for the latter range from three to six months or even longer in some cases. However, most venture capitalists are prepared to give an early indication after receipt of the business plan of whether they are seriously interested in pursuing the proposal.*

### What sort of return will a venture capitalist require?

*Venture capitalists invest in unquoted companies, many of which are relatively immature businesses and thus carry considerable risk. To compensate for this venture capitalists seek high returns, typically of 30-60% per annum.*

**Will investors expect me to sell the business at a later date?**

*The investor's return will generally be provided by a running yield, such as dividends, and a capital return.*

*The eventual sale of the business, whether by sale to another party or by flotation, is the most likely way of achieving the capital returns for both investor and management, although certain investors are prepared to invest for longer terms if conditions are right.*

**The management team can only invest a relatively small amount of capital – how can we retain a significant equity share in the business?**

*Venture capitalists and other equity investors are familiar with this situation – it is a rare exception when management are able to put up more than a minority share of the required funding. This situation may be solved by the use of debt finance, and different classes of equity. Investors are aware of the need to retain the motivation of the management team and will always wish to ensure that they are left with the potential for a return which at least matches that of the venture capitalists, and usually exceeds it.*

*Management are often incentivised by ratcheting the venture capitalist's proportion of the business to management's achievements. A strong performance may result in management retaining a greater proportion of the business.*

**How much cash will management be required to put up?**

*There are no definitive rules on this. In principle, the outside investors will look for a significant financial commitment by the founders/management and in absolute terms this will vary according to the wealth of the individuals concerned. Commitment can of course be demonstrated in other ways. For example, time, effort and money spent in bringing a project to the point when it can be presented to outside investors.*

**What are Financial Covenants?**

*Whilst financiers will often commit funding for a fixed length of time, minimum profit and cash flow ratios may be set by the funding agreement, and investors and bankers may get additional rights if those ratios are not achieved.*

**What is due diligence?**

*This is a term which refers to the investigation and appraisal procedures adopted by venture capitalists and banks prior to making an investment. Such procedures will extend not only to checking out the individuals concerned but also to an examination of all other aspects of the project. Often industrial/technical specialists are employed to help assess the technological and market aspects of a project.*

**Must I have the full management team in place before approaching investors?**

*As management has been identified as a critical issue, it is preferable to have the full team in key areas in place before any approach to investors. However, where gaps exist in the management team these should at least be identified and the steps necessary to fill them outlined.*

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**How do I maintain confidentiality?**

*Where the plan is being produced for external readers, there may be a reluctance to disclose certain information. We recommend that all plans carry a confidentiality clause restricting the use of information therein and that external readers are checked for potential conflicts of interest.*

*It may well be that certain sensitive areas, such as product designs need not be included with the plan merely identifying the benefits derived from the new design.*

**What legal implications exist?**

*Care should be taken when sending a business plan to individuals to ensure that the provisions of the Financial Services Act are complied with and, in particular, that the document is approved as an investment advertisement when necessary. In addition, it is important to have regard to the Companies Act which requires all offers of securities to the public to be accompanied by a prospectus. Copies of the plan should be controlled and distribution recorded.*



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## How Ernst & Young Can Help

If you would like assistance in producing your business plan or are looking to raise finance for a business venture, whether a start-up, a management buy-out, management buy-in, or a development in your existing business, then contact us to discuss your plans.

Ernst & Young is a leading adviser on business planning and raising finance and has strong contacts with the regular readers of business plans, such as venture capitalists, banks and parent companies. Through our extensive experience and knowledge of the marketplace, we can usually indicate which institutions are most likely to be interested in your particular proposal.

You can either contact the partner who usually deals with your affairs or any one of the offices listed at the back of this brochure.

# Products and Production Checklist

- What needs does your product or service satisfy?
- How do competitors satisfy or fail to satisfy those needs?
- What is the impact of customer buying on your product or service? (Are changes in methods, or complementary purchases necessary?)
- What is the reaction to existing or potential customers to your new product/service?
- What is the reaction of your competitors to your new product/service?
- What further research and development is necessary?
- What is the timetable for necessary research and development including testing and regulatory approvals?
- What are the key costs of production or supply?
- What is the critical path of the production process and what are the contingency plans for key areas?
- What is the current production capacity?
- What productivity improvements are necessary to achieve projected growth?
- What capital investment is required?
- What is the production lead time?
- What are the critical aspects of achieving your unique selling point? i.e.
  - quality – quality control
  - delivery time – continuous production
- What is the profitability and cash production of each product?
- What is the likely life cycle of the product or service?
- What development do you expect from competitors, and when do you expect them?
- What protection does your product have?
- How reliable is your product and what are the technical risks?

For services, you will need to focus strongly on the workforce, key attributes, quality control and training.

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## Market Analysis Checklist

- What markets are you currently in, or targeting?
- How big is it now? How big will it be in five or ten years?
- What growth, or changes are shown by third party public reports?
- What are its chief characteristics?
- What are the major trends in the industry?
- Is the industry mature or rapidly changing?
- What are the barriers to entry?
- Who are, or will be, the major customers?
- What companies do you and will you compete with (including future entrants to the market) in each product or service line?
- How do you compare with other competitive companies?
- What is the market share of each existing competitor?

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## Marketing and Selling Checklist

- What marketing strategy will you employ (specialisation, market share objectives, image)?
- Distribution (direct or retail)?
- What promotion and advertising approach will you take (public relations, attendance at trade shows, television, trade magazines)? Will you employ an advertising agency?
- What is your pricing policy (demand pricing or cost-based pricing, volume discounts, show how pricing will change over time)?
- How will you achieve geographical penetration (domestic, Europe, USA, etc.)?
- How will you set priorities among segments, applications, marketing activities?
- Are you targeting increased sales from existing customers or new customers?
- How do you and will you identify prospective customers (both companies, and the relevant decision-makers)?
- What level of selling effort do you or will you have (for example, the number of sales personnel)?
- How efficient is or will the selling operations be (for example, sales per head of sales personnel)?
- What is or will your initial order size be? What is the likelihood and size of repeat orders?
- What is the commission structure for the sales personnel? What does or will the average sales-person earn per year and how long does or will he have to wait to receive commissions?
- For retail operations, where are the shops to be sited? How large are they? How many sales-persons will there be per shop?
- What evidence do you have to back up the above estimates?

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## The Management Team Checklist

- Who are your key managers?
- What are the individual and global objectives of key management?
- How do you intend to retain or attract and compensate key people (i.e. share options, incentive bonuses, etc.)?
- What are their skills and, particularly, their achievements experience, and how does this relate to the success of your venture?
- What management additions do you plan, when, and with what required qualifications?
- Who is on your board of directors?
- What second tier management do you have?
- How many employees do you have and will you require?
- What are your recruitment policies and how will you train new employees?
- Are your employees likely to be affected by any legal, trade or union requirements?
- Show sample organisational structures both current and projected, if significantly different.
- What levels of remuneration do you or will you offer?
- What are the long-term objectives of management?
- What management information system currently supports management?
- What are the key characteristics of the management information system?
- What changes are anticipated to the management information system?

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