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Sources of Financing Small Scale Foundry Enterprise

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Abstract
The government of Nigeria has not paid special attention to Small Scale Foundries (SSFs) industry. Nevertheless, individuals and private investors are involved in producing several thousands of tonnes of castings annually generating revenue for the government through taxation as well as helping with metal waste disposal. Metal cast products are sold both locally and internationally to neighbouring countries. The industry is however faced with numerous challenges. These include access to funding from both government and private financial institutions. To promote this industry, government and private financial institutions must be encouraged to come on board. This paper has looked into the various sources of finance for the development of small scale foundry enterprises. In attempting to look at these sources, the ownership structures of foundry were highlighted. Furthermore, problems that serve as impediments to financing were also mentioned.

Keywords: financing, impediments, foundry, metals

INTRODUCTION

Small Scale Foundries (SSFs) have been in existence for several years in Nigeria. The industry has created several jobs for the people of Nigeria and has minimized the burden on government to find ways of disposing scrap metals generated within the country. While scrap metals are still being exported, the quantity exported has decreased as a result of recycling by foundrymen in producing various parts. The government of Nigeria has not paid special attention to this industry. Nevertheless, individuals and private investors are heavily involved in producing several thousands of tonnes of castings annually generating revenue for the government through taxation as well as helping with metal waste disposal. Metal cast products are sold both locally and internationally to neighbouring countries. The industry is however faced with numerous challenges. These include access to funding from both government and private financial institutions and foundry waste management. To promote this industry, government and private financial institutions must be encouraged to come on board. Foundry process basically consists of making moulds by using patterns, preparing and melting the metals, pouring the molten metal into the moulds, cleaning the casting and reclaiming the sand for re-use. The range of products produced via foundry include manhole covers, pump parts, grinding balls/discs, brake drums, church and school bells, agricultural machinery parts, bronze bushes. For this important sector to contribute to the reformation of our economy therefore, it has to be properly funded. This paper therefore examines the various ownership structures of foundry and attempts to highlight some sources of finance for the development of this important sector in our quest for National development.

Foundry Processing

Foundry is an establishment where ferrous and non-ferrous are first of all melted by the application of heat and made to solidify in the mould to yield solid mass (Plate 1).

Plate 1. Showing the foundry processes at Federal Polytechnic Idah, Kogi State.

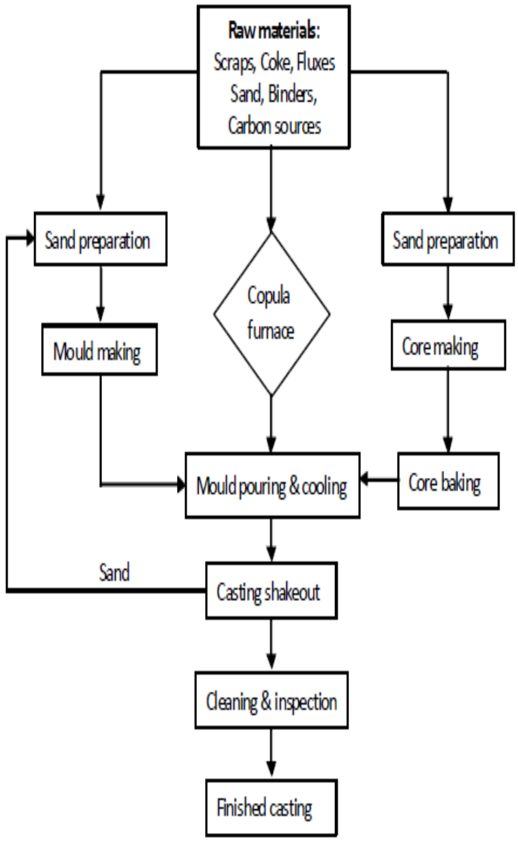

Figure 1.Flow chart of typical casting prosseses.

Types of Foundries

There are many ways of classifying foundries:

i Types of metal cast

a. Ferrous foundry- Ferrous metals such as iron and steel, cast iron.

b. Non-Ferrous foundry such as aluminum, lead, copper, magnesium and their alloys are cast.

ii Types of Mould:

a. Sand casting- Sand mould
b. Die casting- Metal mould
c. Investment casting- Consumable mould
d. Centrifugal casting- Agitating mould.

iii Types of production practiced:

a. Jobbing foundries producing purely on customer's request
b. Captive foundries- Producing for and serving as an integral part of a manufacturing establishment.

Small scale foundries require N1.480,000.00-N28,000,000.00 million. It could be a cottage industry run by members of the family. This type of foundry is highly recommended for rural area.

Foundry industry is a vital basic industry whose important and role is not adequately recognized (Isha, 1987). Foundry find use in automotive industries, large pipe production, large pump housing, valves, hydroelectric plant parts, ship building and a host of many products seen in use everyday.

Out of the numerous manufacturing processes, foundry takes about 80% metal forms and shape produced. This is because of many reasons of amongst which are:

Mass production

Casting is most suitable for quantity production. The basic elements of foundry operations lend themselves to mechanization and automation. Thus, casting may be manufactured with relatively small capital investment. In large foundries, heavy capital investment can be deployed for quantity production and thus low unit cost.

Production of very intricate and complicated objects

No other process offers the same range of possibilities for the shaping of complex features whether in respect of elaborate contours or intricate details which would be impossible or very expensive if any other manufacturing process were to be used other than casing.

Material Composition

Virtually all types of engineering metals and alloys can be cast using the appropriate foundry technique.

Extremely large and heavy objects

Extremely large and heavy objects and shapes up to several tones can be produced by casting.

Ownership Structures

Based on ownership structures, foundries are classified into broad groups (Ibahadode, 1997). These are:

Captive Foundry

A captive foundry is one which is owned by a manufacturing company or some other organization and whose product are manly for consumption of the parent company. A good example of this is the foundry in Ajaokuta Steel Company Ltd.

Independent Foundry

An independent foundry is one which is a separate company or entity that produces casting for any number of customers. Most of the foundries are in this categories. Afoja (2003) reported that most of the foundries in Nigeria fall into the micro/mini category (1-500 tones/year output) while only few produce between 500 and 1000 tones/year (medium scale).One of the major problem facing these small and medium scale foundry enterprises is finance.

Source of Finance

There are several ways through which small and medium foundry enterprises can source for founds. This ways are broadly split into two (Aboaba, 1996):Long-term and Short-term financing.

Long-term financing

Long-term financing needs are those required for the acquisition and development of land and factory buildings, plant and machinery, as well as other fixed structures. Long-term financing include:

Loan

Loans are long-term debt with a maturity of more than one year obtained from banks and specially created financing institution such as Merchant Bank, Nigerian Industrial Development Banks, (NIDB) and National Economic Reconstruction Fund (NERFUND). The purpose of long-term loan is mostly to finance company capital expenditures.

Shares

Share include ordinary and preference share. The ordinary share is a permanent source of capital since they do not have a maturity date. The holder of this type of share is entitling to dividends. The amount or rate dividend is not fixed. Being the owners of the company shareholders bear the risk of ownership; they are entitled to dividends after the income claims of others have been wound up, they can exercise their claims on assets after the claims of other supplies of capital have been met. Preference share is another source of capital. The holders of this share are called preference shareholder. Dividend rate of this share is fixed. Preference shareholders do not share in residual earning. Preference shareholders have claims on income assets prior to ordinary shareholder. They do not have voting rights.

Debentures

Debentures are a long-term promissory note for raising loan capital. The firm promises to pay interest and principal as stipulated. The purchasers are called debenture holders.

Lease Financing

Lease financing is an asset based financing method that can be adopted by an organization. Under lease financing, a contract is entered between the lessor (the owner of the asset) and the lessee (the user of the asset) over an agreed period of time. The lessee pays the rental to the lessor at regular fixed payments over a period of time at the beginning or at the end of the month, quarter, half a year, or year. There are two types of leases:

- Operational lease; these are short term cancelable lease agreements. This type of lease is for convenient and instant services. For example, pay-loader can be leased to move scraps from places of acquisition to firm's scrap yard. In this case, the lessor is responsible for maintenance and insurance.
- Sale-and-leaseback; sale-and-leaseback arrangement occurs when a user sell an existing asset owned by him to the lessor (lease company) and lease it back from him.

Hire purchasing financing

This is an arrangement whereby the owner of the asset (the hire) gives the possession of the asset to the hirer with an understanding that the hirer will pay agreed installments over a specified period of time. The hirer will have the option of terminating the agreement even before the transfer of ownership.

Short Term Financing

Short term financing is the most common type of financing available in the market. Short term financing include:

Commercial and Merchant Banks

The commercial and merchant banks have agreed to the monetary and credit policy of the Central Bank of Nigeria (CBN) which urged both banks to set aside 10% of their profit before tax for financing of projects in the small and medium-scale enterprises. The exercise which started in 1999 financing year has enable banks to invest N2.87 billion in 49 projects. Mordi (2003) reported that N14.6 billion has been pooled into the small and medium industries equality investment scheme (SMIEIS). Below the SMIEIS initiative in August 2001, Merchant Banks had been encouraging entrepreneur in Nigeria. The Federal Office of statistics (2000) reported a total disbursement of N589.89 million between 1991 and 2000 to encourage entrepreneurs in Nigeria.

Short term loan/overdraft financing

Overdraft financing is provided when business makes payments from their business current account exceeding the available cash balance. An overdraft facility enables business to obtain short-term funding although in theory the amount loaned is repayable on demand by bank.

There are several important factors to consider when assessing the appropriateness of an overdraft as a source of founding SME's;

- The amount borrowed should not exceed the agreed limit. The amount of the facility made available is a matter of negotiation with the bank.
- Interest is charged on the amount overdrawn at a rate that is above the Bank Base Rate. The bank may also charge on overdraft facility fee.
- Overdrafts are generally meant to cover short-term financing requirements they are not generally meant to provide a permanent source of finance.

Love Money

Love money can be defined as own capital love money embodies informal finance from relatives or friends given to an entrepreneur one knows in person, often a younger member of the family, to start or to develop an activity. The most important feature of loving financing is the personal effective relationship between the provider of the finance and the entrepreneur.

Business Angels

Business Angels are another source of informal finance that early stage enterprises attempt to draw on. They are wealthy individuals with substantial business and entrepreneurial experience who are prepared to take as take-in enterprise. Although they can step in at any development stage, Business Angels invest predominantly in start-ups and seed-stage ventures; they are not interested in transfer of business but in innovative investments. They are extremely selective, and generally require the recipients of their investment to have high growth potential.

Why do Small and Medium Foundry Enterprises (SMFE's) find financing a problem?

The main problem faced by SMFE's when trying to obtain funding is that of uncertainty:

- SMFE's rarely have a long history or successful track record that potential investors can rely on in making an investment
- Larger Companies (particularly those quoted on a stock exchange) are required to prepare and publish much more information which can actually assist the finance raising process; Because the information is not available in other ways, SMFE's will have to provide it when they seek finance. They will need to give a business plan, list of the company assets, details of the experience directors and managers and demonstrate how they can give providers of finance some security for amount provided.
- Banks are particularly nervous of smaller business due to a perception that they a greater credit risk.
- A common problem is often that the banks will be unwilling to increase loan founding without an increase in the security given. One thing all loan source have in common is that they are selling their money, not buying your project (Walker, 1982).

CONCLUSION

The survival of any developing economy hinges on how well the small and medium foundry enterprises are supported. No nation can achieve industrial growth and economic development without stimulating small and medium scale enterprises. As a catalyst for development, they launch the economy into an industrial giant. Small and medium scale enterprises despite some of finance highlight should be adequately financed to ensure the economy growth/development of the nation.

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