A Report of Financial Issues Related to Setting-Up a New Manufacturing Unit

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Executive Summary

It is essential for an organization to be commitment in order to get started with a manufacturing unit. Expanding manufacturing set up requires careful planning. It also requires considering each aspect in which investment needs to be made. Careful scrutinization of various aspects where finances are involved is the most important requirement. Based on the analysis of the various financial issues and their solutions the feasibility to start a new manufacturing project would be undertaken.

In Ruritania, almost all the aspects are in favor of setting up a manufacturing unit. But inspite of this there a number of financial issues that needs to be considered. The various issues comprise of aspects related to manufacturing startups, sourcing of funds, usage of capital reserves, human resource management issues, marketing management issues, production and logistics management issues, communication and coordination issues and finally issues related to miscellaneous and hidden expense. Finances are required to resolve all these issues. Thus it is essential for any organization to identify ways to effectively and efficiently use its finances so that overall organizational profitability is ensured and organizational goals are achieved.

In this report, the various financial issues that will be encountered by the company to set up a new unit in Ruritania are outlined. Various recommendations are also outlined in order to overcome these issues. At the end of the report a brief financial plan in outlined which is followed by a conclusion.

No report is error free thus there is a probability of errors in this report which is acceptable.

Brief Company Profile and Decision Overview

The company is into the business of manufacturing automobile parts which are mainly supplied into automotive industries. Thus the customers of the company comprises of industrial units. The company mainly operates in United Kingdom with a market capitalization of 600 million GBP.

The decision under consideration is to identify the various financial issues related to set up a new manufacturing unit in Ruritania by the company.

In this era of globalization and stiff market competition it is essential for all organization to plan expansions. Expansion of manufacturing unit by this company was an obvious choice but it is also essential to consider the various issues related to this expansion plans.

Financial Issues

In order to start up a new manufacturing unit in Ruritanian the organization has to face a number of financial issues. The various financial issues are summed up in the following paragraphs.

Manufacturing Start-Up Issues: In order to set up a new manufacturing unit it is important to make investments that are fixed in nature. While setting up a new manufacturing unit in Ruritania is a very ideal option for the company but yet the company has to ensure locking of funds in form of investment in fixed assets like land, building, machinery, equipments, furniture and fixtures. These investments once done will lock up organizational funds thus making it difficult and time taking for the company to liquidate. Further the unit will also have to invest in raw materials. Though these raw materials can be liquidated more easily but yet the company will have to lock its investments.

Capital Reserves: One of the most important financial issues that needs to be taken care of availability of capital reserves. For any organization in order to start a new manufacturing unit it is essential to bear start up costs for which any company is prepared. But as soon as the operation starts, the unit will experience operational costs. Initially these operational costs are very high as the unit is new. With the passage of time the unit will mature and thus will be in a position to manage operational costs. Even analysts have clearly pointed out that until 2 to years of operations; no unit is in a position to churn out profits. Thus in order to ensure this unit's survival in the long run and provide for organizational sustainability the company needs capital reserves. As the operational costs of the new unit till a certain period of time will result in added on costs for the whole organization it is very challenging to have a high amount of capital reserves. This capital reserve is essential to ensure that till the time this new manufacturing unit does not help the company to earn profits, all hiccups experienced by the unit is taken care of. Maintaining such a huge financial reserve is an issue for the company.

Issues related to Raising Funds: The company is in a position to completely finance the project. But still it is also essential to consider the various options of raising funds. These comprise of external sources like banks, private investors, loans from other financial institutions, share markets etc. But deciding on optimum combination of capital is one of the most crucial decisions that needs to be taken. If wrong choice is made and the company lands up arranging finances from inappropriate sources then it will result in increasing organizational losses and costs. Thus raising funds is an important issue that needs to be considered logically.

Production Issues: While setting up a new manufacturing unit, it is obvious that it would result pressures of organizational profitability. It is mainly in as there will be no profits and the company will experience increased costs. In order to ensure production the company will have to meet various direct and indirect costs (Leachman, Pegels, & Shin, 2005). Out of these costs some are electricity, labor, tools, rent, wages etc. The company will have to ensure availability of funds to meet these recurring expenses. Irrespective of production size and volume, the company has to bear fixed costs. But variable costs are dependent on the volume of production. As both fixed and variable costs make the total costs of an organization, it is essential to control both. Labor skills are another important aspect that needs to be considered. Though labor is cheap in Ruritania but if inappropriate labor is used then that would result in wastages of raw materials and early depreciation of tools, equipments and machineries. Thus resulting in production bottlenecks and added organizational costs.

Logistics Issues: Logistics form a core part of organizational costs. It is related not only to the movement of finished products but also movement of raw materials (Poon, Choy, Chow, Lau, Chan, & Ho, 2009). Further it does not only include movement of raw materials and finished products from outside the organization to inside organization. But it also includes movement of raw materials and finished products within the organizational premises. If logistics are planned properly then raw materials and finished products may be mishandled resulting in wastages, damages and added movements of products (raw materials) thus resulting in increased costs. The company has to make investments in designing logistics strategies and arranging equipments that would provide for cost effective movement of gods and products. This requires careful investment planning.

Marketing Issues: Though the marketing expenses are not very heavy in the initial phase but with the passage of time the organization will have to undertake extensive marketing strategies which will require heavy funds. As the company already has a marketing set up thus initially it may not undertake marketing expenses. But in order to sell the new increased output efficiently and profitably across the target customer segment it is essential to develop elaborate marketing strategies which require investment commitments. (Kotler, 2009)`

Human Resource Management Issues: In Ruritarian though the human resources that is labor is available cheaply but yet it is essential to consider other human resource management aspects too. But other than manufacturing labor it is essential to have management staff and other employees at supervisory level. Further as the employees will be new in the new manufacturing unit it will be essential for the company to organize for training and development programs. This will help the organization to enhance employee efficiency to match the organizational levels. This requires additional investments.

Communication and Coordination Issues: The new manufacturing unit is not closely located to the headquarters in United Kingdom. This is the first venture of the company outside United

Kingdom. In order to ensure efficiency and effectiveness of new unit it is essential to closely monitor and control its activities. Further if there is absence of effective communication and coordination set up within the various units of the organization then organizational performance declines thus resulting poor performance of the company in the markets (Walter, Lechner, & Kellermanns, 2007). This requires effective communication and coordination set up which leads to additional investments. This will add to the existing organizational costs thus suppressing organizational profits. If the company fails to maintain effective and efficient communication and coordination between the new unit, existing units and its headquarters then the new manufacturing unit may result into a failure.

Miscellaneous Expenses: Some of the expenses that are generally not accounted for while designing plans and strategies for setting a new manufacturing unit in Rutitanian comprises of legal fees, licensing expenses, social compliance expenses, social developmental and benefit expenses any other professional fees. These expenses are incurred in due course of time and are considered as hidden costs. These costs form a considerable part of the investment and thus should be accounted for. (United Nations, 2002)

Recommendations

Manufacturing startup issues are faced by all organizations irrespective of its size, industry, location and experience. Thus careful planning of investments is essential to avoid wrong investments. Further it is also required that the production departments along with other technical heads discuss in details and develop a plan related to start up investments. The company should minutely scrutinize all the possible options before finalizing the investment decisions. The company needs to develop an appropriate cash flow statement that should provide for accurate estimations thus helping the company manage start up costs and investments. (Biz Filings, n.a)

In order to overcome the issues related to financial and capital reserves required to for the organizational management to create capital reserves funds specifically for this purpose. Further the company can also develop a start-up budget which contains higher estimated costs so that this fund can be utilized to meet operational costs of the new unit. The financial team also needs to develop an accurate break even analysis for the new unit so that a clear estimation of operational costs can be made. The break even analysis will help the company to identify the time from which this new unit will add to organizational profits (Palmberg, 2006). Thus it will in the overall planning of the organizational strategies.

The company should very closely scrutinize all the opportunities of availing finance. Based on detailed analysis and opinions from expert sources like financial analysts and industrial analysts the decision with respect to sourcing of funds must be undertaken. This will help the company to develop an optimum capital ratio thus helping to derive maximum benefit from the same (Zhang, 2013).

The various production related costs can be managed through appropriate cost accounting. The company needs to identify various costs and provide for appropriate accounting for the same. The company should schedule its production to realize economies of scale. This will help the company to minimize total costs rather than working on individual cost elements. (Hansen, Mowen, & Guan, 2009)

It is recommended that the company to design marketing strategies that would help the company to create new markets and a buzz in the existing markets with respect to products that is to be manufactured. This will result in immediate sales of the products thus ultimately resulting in immediate realization of revenues. (Thomas, 2004)

To provide for effective communication and coordination the company can adopt for information management systems and intranet. Though this requires huge investment but this investment is one time but would provide for benefits for a long period. This would result in effective and efficient communication and monitoring of activities. This will also help in quick and yet effective decision making (Nonaka & Konno, 2005).

Financial Plan Highlights

As financial plan is just estimation, it is developed considering certain assumptions. The various assumptions considered in developing financial plan outlines are:

- The environmental factors like political conditions, customer demand, market conditions, competition structure, banking and financial systems and trends, international business environment are steady
- There is no change in consumer purchase pattern and choices
- Costs are incurred as projected and estimated
- Euro has been adopted by Ruritania
- The international exchange rates are stable

The main revenue of the company will be from the sale of final outputs (Needles, Powers, & Crosson, 2010). This will comprise of parts for automobile products. Some of the parts will be standards ones and others will be customized. The gross profit margin of the company will be approximately 25% in the first year and will increase eventually to 45% in the 2nd year. The new manufacturing unit will reach its break even by the end of its first year. So from 2nd year it will be earning net profits also. Net profit margin will range from 10% to 16%. Gradually these profit margins will increase.

The total capital requirements for setting up the new manufacturing unit that is 55 million GBP will be met through four major sources. One is though floatation of new equity shares that is 30 million GBP. Second through business loans that is 10 million GBP. Third through outside corporate investors that is 7.5 million GBP and fourth through organizational funds that is 7.5million GBP. Maximum funds will be raised through outside. These funds will be used to meet the start up expenses and will be invested in fixed assets. The other recurring expenses, operating expenses and variable expenses will be met through company's capital reserves.

The above financial details are just outlines based on the prepared by financial manager along with financial team.

Conclusion

Finances form a very crucial aspect to start a business. It is mainly because it is money that decides the present and future of a business. Thus proper financial planning is essential so that the organization does not fail to meet its objectives. Many organizations fail inspite of having the best of the manufacturing idea and the best of the strategies as they are not in a position o manage their finances well. Setting up a new manufacturing unit in Ruritania in such idealistic situations requires careful thinking. The unit will be successful if it is in a position to overcome all financial hurdles successfully and deliver the best possible results to the organization. Thus the success of the new manufacturing unit will be determined based on its contribution towards organizational profitability and sustainability. The various recommendations if properly executed will not only help the manufacturing unit to overcome various related financial issues but also enhance organizational viability in the long run. It will also help the company to further expand its business and set up manufacturing units in other parts of the world. This will help the company to emerge as an international company catering people across the globe.

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