

CHAPTER - II

INDUSTRIAL SICKNESS IN

SMALL-SCALE INDUSTRIES.

INDUSTRIAL SICKNESS IN SMALL SCALE INDUSTRY

Several studies have been made to determine the extent and the causes of sickness in small scale industry. A brief review of the various studies is given below.

STUDY TEAM REPORT OF THE STATE BANK OF INDIA (1975)

The study Team of the State Bank of India headed by Shri J.S. Varshneya examined 120 small scale units with aggregate borrowing in excess of Rs. 2 lakhs. The study team found that 100 units were in the unsatisfactory group and barely 20 were in the success group.

Among the factors which were responsible for extensive sickness, the most important was lack of management expertise and lack of adoption of sound business principles in running the enterprise. This was evidenced by the fact that the units did not evolve healthy principles of functioning in key functional areas, such as finance, marketing and production. This was corroborated by the following findings :

- i) Most of the units had a poor equity base and this limited their capacity to overcome difficult times.
- ii) Established units, even during periods of good business did not make an effort to build up internal financial strength to provide funds for contingencies.

They exercised no financial discipline and thus committed their funds in various medium-term investments or increasing overheads and thus the liquid funds needed to meet the requirements of current liabilities fell short in supply. This resulted in difficulties.

- iii) Once a unit was in trouble, it got further into trouble by working in panic and thus resorted to borrowings at high interest to overcome its short-term difficulties. In the process, it went deeper into trouble and failed to extricate itself.
- iv) The units lacked experience in both technical and/or managerial ability.

ENTREPRENEURIAL DEVELOPMENT PROGRAMME IN GUJARAT

The study covered 248 units in Gujarat which were considered to be performing unsatisfactorily. The study highlights the fact that managerial inexperience was the most significant cause of failures in small-scale industries.

The study revealed the following :

- i) Performance of the enterprise is positively associated with the age of the entrepreneur. As the age of the entrepreneur improves, performance also improves.

33 per cent of the technicians in the below 20 age group performed unsatisfactorily while only 17 per cent in the above 40 age group performed similarly.

The failure rate among the college drop-outs was as high as 56 per cent.

63 per cent of the students performed very poorly as entrepreneurs.

Performance of professionals covering managers, senior executives, professors, etc., was very commendable as the failure rate in this category was only 9 per cent.

Those with 5 years or more experience did better, while those with no experience or nominal experience did the worst with 24-25 per cent failure.

- ii) Labour problems were the least important causes of failure in small-scale industries, though labourers were the worst sufferers in the process.

SURVEY OF MORTALITY OF SMALL-SCALE UNITS IN SOUGH INDIA

H.K. Mazumdar and A. Nag of the Indian Institute of Economics, Hyderabad, conducted a survey of the non-existing units in the States of Andhra Pradesh, Kerala and Karnataka to study the causes of mortality among the small-scale units registered from 1959 to June 1975. It was revealed according to the Census of Small-Scale Industries that deaths of 18,483 small units took place during the period. Out of them, a sample of 1,750 units was surveyed for the period September 1974 and March 1975. The findings of the study completed in December 1976 revealed the following :

- i) More than 40 per cent of the dead units in each of the States of Andhra Pradesh, Kerala and Karnataka did not have a life span of more than two years; that 25 per cent of the units died in the second year and about another 20 per cent in the third year. In other words, the infant mortality rate was very high among the small enterprises.
- ii) Dead units are characterised by low employment levels and average employment in about 60 per cent of the dead units did not exceed five and in about 90 per cent of the units did not exceed nine.

- iii) The dead units suffered heavily on account of under-utilisation of capacity. This was chronic feature since average utilisation of capacity was as low as 36 per cent. Three factors accounted for under-utilisation of capacity : lack of finance to meet working capital needs, lack of demand and non-availability of adequate raw material supply.
- iv) A very high ratio of inventories to total production was observed among these units. In Andhra Pradesh and Kerala, inventories were 54 per cent and 48 per cent of total production.

STUDY OF SICK UNITS IN VIDARBHA :

Vidarbha Industries Association published a study of 50 sick units having capital investment ranging between Rs.1 lakh and Rs. 5 lakhs. The study concluded : " That most of the difficulties of small-scale units arise from financial and administrative rigmarole; that spiralling interest charge and recession in demand tend to make units sick; that requirements of credit of small scale units located at a far away place would be higher than those located at an industrial centre because they have to maintain higher inventories; and that institutional financial agencies have failed in acting as sentinels of progress, growth and employment."

HARYANA'S STUDY OF SMALL SCALE UNITS :

The Haryana Unit of the All India Federation of the Small and Rural Industries in their memorandum submitted to the Union Minister of State for Industries on 14th April, 1979 has pointed out that one of the basic factors responsible for sickness of small units is the fact that most of the 'principals' do not pay the ancillaries for six months or even longer after the purchase of goods. If the ancillaries dare protect against erratic payments, the principals threaten to stop purchasing from them. The Memorandum drew attention to the blatant though sad reality : "Nearly 60 per cent of the 'sick' small and rural units would not have gone sick had the principals not delayed the payments 'for more than four months'. Of the 9,064 ancillaries that supplied spares worth Rs. 900 crores to the Principals in and outside Haryana during 1978-79, according to an official tally, barely 632 units received payments within 90 days of delivery. Over 3,000 ancillaries received the payments within three and six months, and that too after repeated personal and postal reminders."

"Every fifth 'principal', according to this tally, fails to honour the commitment regarding the date and mode of payment to the ancillary. In about 1,000 cases, the principals have not yet paid in full for the products supplied over a year ago."

According to another statistical study, "nearly 80 small and tiny units (commonly called unorganised sector) close down every year merely on account of labour trouble caused by non-payment or short and delayed payment of salaries to the workers."

PRINCIPAL FACTORS RESPONSIBLE FOR SICKNESS OF SMALL UNITS :

A review of the various studies regarding small-scale units reveals that the following factors account for sickness in them :

- i) A very important factor is the lack of management expertise. Young entrepreneurs start enterprises with romantic ideas. They keep high overhead costs, borrow at high rates of interest and do not care for making economies in costs, more especially during the period of infancy. Thus, inexperienced management of small units is one of the important causes of sickness.
- ii) Non-observance of the basic principles of business management is another major contributing factor to sickness. To start enterprises with a low equity base, to make no effort to build internal financial resources during good years, to maintain high inventories to total production, to invest short-term borrowings in medium-term investments, etc. result in developing poor internal resilience to fight difficult times.

- iii) Under-utilisation of capacity caused by lack of working capital, lack of demand and non availability of raw materials results in industrial sickness, leading to the death of small enterprises.
- iv) Easy approval of small-scale units by the State without proper screening of project proposals also resulted in sickness. This only under-scores the fact that assessment of viability of the projects is not made with adequate care, more especially with regard to financial viability. This explains why infant mortality rates among small scale units were higher during the second and third year.
- v) The dead units depended mostly on their own funds, i.e. on their individual savings, rather than on borrowed funds. Among the dead small units, own funds accounted for 89 per cent of gross investments. For working capital requirements, these units depended on nationalised banks or co-operative banks.
- vi) Non-payment by the 'principals' to the ancillaries has been noted as an important cause of industrial sickness in Haryana.

MEASURES TO PREVENT SICKNESS IN SMALL UNITS :

The problem of industrial sickness in small units has to be treated differently from the problem of sickness of the large units. It is basically the problem of increasing the competitive strength and viability of the small units. For this purpose, the following measures deserve consideration :

- i) The Reserve Bank should issue guidelines for the operation of small units and thus make depreciation, retained profits and expansion programs so as to build their internal financial strength.
- ii) The Government can institute a comprehensive monitoring system which should make the submission of monthly returns by the sick enterprises compulsory. In this way, the misuse of funds for purposes other than specified, and the factors leading to low capacity utilisation can be examined and quick remedial action taken.
- iii) The Government can accord priority in allocation of scarce raw materials, extending marketing assistance and granting certain rebates and concessions to small units and more so to such units which show better records of performance.
- iv) Sickness of small units should be treated at par with scarcity/famine in agriculture and thus concessional

rates of interest be charged at par with those loans that are granted in scarcity/famine conditions in agriculture. The maximum rate of interest should be 7 per cent for small sick units to enable them to secure soft credit.

- v) The Government should not accept the suggestion of having separate minimum wage rates for the small units and the large and medium units. In fact, in the small units the entrepreneurs have been forcing labour to accept less than the minimum wage and sign for the full rate. With the growth of trade unions in small units, the entrepreneurs find it difficult to extract this illegitimate gain. The basic principle that any unit which can not pay minimum wages does not have the right to exist, ~~has~~ to be accepted. Instead of this, the more important solution would be to make the units viable.
- vi) The Government should take penal action against the principals for non-payment for the delivery of goods by small units. The Government should endeavour that the ~~small~~ enterprises do not become the underpinnings of the large enterprises. The disciplining of large enterprises is a sine qua non for the rehabilitation of the small enterprises.

A suggestion has been given in this respect by the President of Haryana unit of the All India Federation of the Small and Rural Industries that the banks should advance low-interest capital to the ancillaries against goods supplied to the principals and the repayment of this low-interest capital should be linked up with the payments made by the principals. This suggestion is a defeatist one. It silently accepts the waywardness of the 'principals' to pay as and when they please, but calls upon the State to provide low interest loans to small industries so that they do not develop sickness. To the extent, it helps the small industries it is welcome but acquiescence with the 'principals' will further encourage them to delay payment in the hope that the State will come to the rescue of the small units. The defaulting principals have, therefore, to be brought to book.

vii) Since a majority of sick units die in the second or third year of their existence, a programme of monitoring and nursing them during infancy is very essential.