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CHAPTER - II  
SMALL SCALE INDUSTRIES  
THEIR NATURE AND PROBLEMS AND  
SMALL SCALE INDUSTRIES  
IN KARWAR TOWN  
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## CHAPTER II

### SMALL SCALE INDUSTRIES, THEIR NATURE AND PROBLEMS AND SMALL SCALE INDUSTRIES IN KARWAR TOWN

#### 2.1 INTRODUCTION

Small Scale Industries have gained a unique position in the economy of a country. This is true in the case of both developed and developing countries. This unique position is gained because of their advantages over large scale industries. It is necessary to clarify the meaning and importance of Small Scale Industries and also about the types of finance required before the financing of Small Industries is studied.

#### 2.2 MEANING OF SMALL SCALE INDUSTRIES :

The concept of Small Scale Industries does not seem to lend itself to scientific definition and therefore vagueness and lack of exact delineation permeates the literature in this area.<sup>1</sup>

Definition of Small Scale Industries have varied depending on the basis adopted whether it relates to quantifiable parameters like the amount of capital invested or the number of persons employed or to qualitative norms like the use of low-level technologies or low degree of specialisation in administrative and management function.<sup>2</sup>

The Small Scale Industries are defined differently in developed and developing countries.

In the U.S.A., a developed country, Small Scale Industries are referred to as Small Business. The Small Business Administration defined Small Business as follows:

In retailing a firm is considered small if its annual sales do not exceed 2 million.

Among Service Firms, a firm is considered small if its annual receipts do not exceed \$2 million.

In Wholesaling a firm is considered small if its total annual sales do not exceed \$ 9½ million.

In manufacturing a firm is considered small if it does not have more than 250 employees.

In transportation and warehousing a firm is considered small until its annual receipts exceed \$ 1 million.

In construction a firm is considered small unless its income exceeds \$ 5 million for the immediately preceding three years.

( The amounts change year after year due to inflation.)<sup>3</sup>

In Japan, another developed country, Small Scale

Industries covers manufacturing units employing less than 300 persons or having capital investment of less than 10 million yen.

In Sri Lanka, a developing country, Small Scale Industries is defined as a unit using power and having capital investment in land, building and machinery, not exceeding Rs. 5 lakhs.

In Pakistan, another developing country, Small Scale Industries is defined as a unit having Rs. 7.5 lakhs in fixed assets.<sup>4</sup>

Thus, in other countries also Small Scale Industries are defined differently. There is no one apt definition of Small Scale Industries to one country at all times.<sup>5</sup>

After considering the definitions of Small Scale Industries, in other countries, now let us turn to the definition of Small Scale Industries in India.

In India Small Scale Industries is a broad concept covering within its ambit any industrial activity carried on by a person or a group of persons including technically qualified entrepreneurs or artisans.

The definition of Small Scale Industries in India has been changed from time to time. The following definition is applicable since 1985.

" A Small Scale Industry is an undertaking having

invested in plant and machinery, whether held on ownership basis or by lease or by hire purchase, not exceeding Rs. 35 lakhs. This also includes an ancillary industry having investment in fixed assets in plant and machinery whether held on ownership basis or by lease or by hire purchase not exceeding Rs. 45 lakhs and engaged in-

(a) The manufacturing of parts, components, sub toolings or intermediate; or

(b) The rendering of services and supplying or rendering or proposing to supply or render 50 percent of their production or the total services, as the case may be, to other units for production of other articles.

Tiny industries form part of Small Scale Industries and are defined as follows:-

" The Tiny sector Industrial Unit is a unit located in villages and towns with population not exceeding 50,000/- ( as per 1971 Census ) and in which the original investment in equipment and machinery does not exceed Rs. 2 lakhs.

The tiny industrial units which cross the investment limit as a result of expansion shall cease to enjoy the special incentives meant exclusively for tiny sector from such date of crossing and hence forward shall be eligible for incentives meant for small scale

units.<sup>6</sup>

It is obvious from the definition of tiny industries that the intention of creating tiny sector is to encourage them by giving them special incentives. The tiny industries lose special concessions once they grow into small scale industries, but will get the concessions available to Small Scale Industries. Thus, in reality, tiny industries are part of Small Scale Industries.

Though cottage industries also have less capital investment and are run on Small Scale, they are different from Small Scale Industries. Cottage Industries are mainly carried on in the residence of proprietor. The production is more manual and use of machines is comparatively limited. They are mainly sole proprietorship firms. Small Scale Industries may be organised by partnership firms and joint-stock companies.

The Planning Commission has classified Small Scale Industries as-

- (a) Traditional Industries which include Khadi and Village Industries, Sericulture and Handicrafts. These industries are generally artisan based, located mostly in rural and semi-urban areas.
- (b) Small Scale Industries having certain degree of technological sophistication. They are generally

located close to or in the urban areas.<sup>7</sup>

From the definitions referred to above the following characteristic features of Small Scale Industries emerge.

- (1) The Small Scale Industries are mainly located in Urban and Semi-Urban areas.
- (2) They generally use machines, power and sometimes apply modern techniques of production.
- (3) Their capital investment in plant and machinery is not more than Rs. 35 lakhs. In case of ancillary Industries this limit is raised to Rs. 45 lakhs while in case of tiny Industries this limit is only Rs. 2 lakhs.
- (4) The Small Scale Industries operate in a compact area. They do not reach a large market.
- (5) They employ limited number of workers, many units are so small that they carry on without having any worker. All work is done by owner himself.
- (6) They cater to individual tastes and fashions.
- (7) They render personalised service.
- (8) They are flexible and adopt to changing tastes fashions.

### 2.3 IMPORTANCE OF SMALL SCALE INDUSTRIES IN INDIA.

Small Scale Industries are useful when new products

have to be essentially produced on a small scale as there is no established demand for them. The owner of the small firm can work hard for making the new product or idea successful which may not be possible for the employees of large business house.

The Small Scale Industries have an edge over large business houses in circumstances where the personal attention of the owner is essential to daily operations. The owner can easily look into the various aspects because in most of the cases the owner himself carries on operations and can easily supervise the Small number of workers in his organisation.

The Small Scale Industries are better suited where personal services, either professional or skilled are dominant. The entrepreneur of a Small Scale Industries can provide such personal services better than the employees of a large scale industry.

The Small Scale Industries are advantageous when the market for the product or the service is mainly local. The demand for the product or the service being limited, Small Scale Units can fare better than large scale units.

The Small Scale Industries have low capital/ labour ratio. "For a modern Small Scale unit on an average an investment of about Rs. 7,000/- is required



for creating one work-place while in a large sector unit the investment per work-place is about eight times this amount.<sup>8</sup>

Small firm is useful when it deals in perishable materials or articles. Due to better transport facilities even large concerns can enter the market for perishable materials or articles. But still the small firms can supply fresh materials or articles. But still the small firms can supply fresh materials or articles and thus score over large industries. In the face of competition from large bakery concerns, the small bakeries have survived in almost every town.

Small Scale sector is considered as elixir for all the ills of a developing economy like ours. This sector has been assigned crucial role to play in the 7th Plan.<sup>9</sup>

Small Scale units cater to the specific needs of the market with better feel of the market situation.

They are better suited when the market for the commodity manufactured is small and cannot be increased.

Encouragement of Small Scale Industries in backward areas can bring about balanced regional development. They can use unskilled/semiskilled labour available, in backward area.

Small Scale Industries are the proper answer when the industry is characterised by wide variations

in demand or styles. The small concern can adjust easily to the fluctuations than the large concern.

Small Scale Industries are better when close rapport with personnel is essential. In a small concern the number of employees being limited, a better rapport with them can be easily established.

Small Scale Industries are particularly useful in rural India. Disguised unemployment is a major feature of rural India. The man-land ratio is very high. Small Scale Industries help to provide employment and reduce disguised unemployment and man-land ratio.

Small Scale Industries assist in reducing inequalities of income. While large industries tend to develop concentration of economic power in a few hands and promote inequalities in the distribution of income, Small Scale Industries have just the opposite effect.

Small Scale Industries provide employment opportunities better than large-scale industries. Small Scale Industries had only 7 percent share in the total fixed capital investment of all factory establishments. But they provided 36 percent of total factory employment.

The managerial skill of a very high quality is always in short supply. The Small Scale Industries do not require such superior managerial skill. The social cost of Small Scale Industries is low. Big industries create problems like shortage of accommodation water pollution

etc. Small Scale Industries are decentralised and have low social cost.

#### 2.4 PROBLEMS OF SMALL SCALE INDUSTRIES IN INDIA :

The entrepreneur has to face several problems in establishing and running a small scale unit. "The Small Units suffer from many inherent weaknesses in comparison to the large scale industry. The small enterprises are more flexible than the giants, but are highly vulnerable to any set backs".<sup>10</sup> Deciding the place of business, procuring of raw-materials, marketing of production and financing all these activities are some of the problems. Of these financing is a major problem.

#### 2.5 FINANCE :

Finance is a major problem of Small Scale Industries mainly because-

- (1) Internal sources are less. Small Scale Industries is established mostly as a sole-proprietorship concern where a single person has to bring in finance. The ability to bring in own capital is less.
- (2) Capacity to borrow also is less because own investment of the proprietor is less. The total capital available is not sufficient to carry on business. This shortage of capital forces the concern to carry a business on a level which may be uneconomical.

- (3) As interest is to be paid on the borrowed capital the surplus generated is less. This also affects the ploughing back of profit.
- (4) There is no surplus finance to live on during the period of strain.

Finance is regarded as the king-pin of business enterprise. It is defined as the provision of money at the time it is wanted.<sup>11</sup> Wheeler in his "Business-An introductory analysis" defines finance as follows-

"Business Finance is defined as that business activity which is concerned with the acquisition and conservation of capital funds in meeting the financial needs and objectives of business enterprise".<sup>12</sup>

Thus finance is required to acquire assets and meet other day-to-day expences. A Business unit requires fixed assets as well as current assets. Fixed assets are the assets acquired for using in the concern and not with the intention of transferring them and converting them into cash. Plant and machinery, furniture and fittings and such others are fixed assets required by a business concern.

The assets are such that cannot be withdrawn without disturbing the normal working of the undertaking.

Current assets are the assets which will be turned into cash within a short period of time. They are required for continuous operation of business. One form of assets

changes into another. Raw-materials, stock-in-trade, debtors, cash-in-hand and bank are examples of current assets.

A Small Scale Unit requires both fixed assets and current assets in right proportion. The amount invested in fixed assets is fixed capital. Shubin in his book ' Business Management' defines fixed capital as " the funds required for the acquisition of those assets that are to be used over and over for a long period, such assets as land, buildings, machinery, equipment and tools".<sup>13</sup>

The amount invested in the current assets is working capital. It is also called Gross Working Capital. Net working Capital is the amount obtained by subtracting current liabilities from Gross Working Capital. Creditors, Bank overdraft Bills payable and such others are current liabilities.

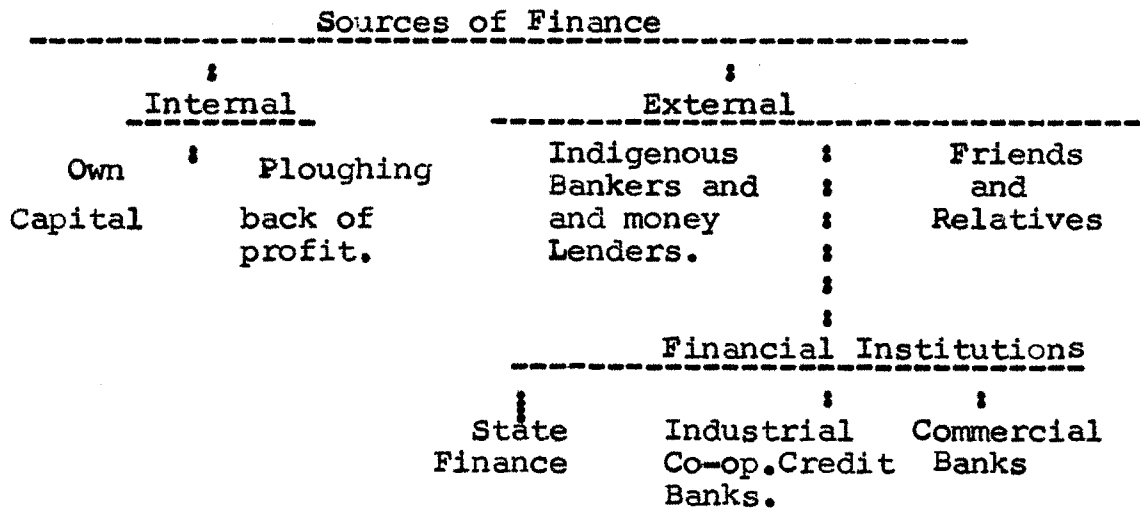
Having noted the meaning and types of finance, it is necessary to turn to the study of sources of finance.

## 2.6 SOURCES OF FINANCE :

The required finance may be obtained by a Small Scale Industries from several sources. These sources may

be classified as : (1) Internal sources and (2) External Sources.

- Chart 2.1 showing sources of Finance -



#### 2.6. INTERNAL SOURCE : OWN CAPITAL :

Also called equity capital and risk capital it is the amount contributed by proprietor in the case of sole-proprietorship, partners in the case of partnership firm, and shareholders in the case of joint-stock company.

It is an absolutely necessary source of finance. In the case of Small Scale Industries the amount of own capital will be less because most of the Small Scale Industries are established as sole proprietorships where only one person has to bring in capital.

#### 2.6.2. INTERNAL SOURCE : PLOUGHING BACK OF PROFITS:

A part of the profit earned may be retained in the firm and reinvested in the business of the firm.

This is in the form of reserve and may be regarded as part of own capital. It is part of the profit which actually belongs to the Proprietor. But this source has limitations. The finance available depends upon the profit made and the percentage of profit set aside.

#### 2.6.3 External Source : Relatives & Friends :

A sole proprietor may get funds from his relatives and friends, usually without interest. The terms of repayment are not certain and hence may be used for both long-term and short-term. However the friends and relatives may demand their money back at any time and hence it is not reliable. Also, they may assist once or twice, usually at the commencement of business, but may not help arunning concern.

#### 2.6.4 External Source :

##### Indigenous Bankers and Money Lenders :

The indigenous bankers can be easily approached and the procedures to be followed are simple. But the rate of interest is very high. Also the loan is available for short period only.

#### 2.6.5 External Source : Financial Institutions :

The Financial Institutions provide long-term and short term loans to meet the various financial needs of a business unit. The term Financial Institution has a very wide meaning and it includes all the Financial

Institutions operating on capital market and money market. But for the purposes of Small Scale Industries. The term includes:

- (a) State Financial Corporations,
- (b) Industrial Co-operative Credit Banks and
- (c) Commercial Banks.

They provide finance to meet fixed and working capital needs of Small Scale Industries. The rate of interest is reasonable and low compared to indigenous bankers and money lenders.

Considering all these sources of finance for a Small Scale Industries, the two sources which stand out are : (1) Own Capital and (2) Borrowed capital i.e. borrowing from financial institutions. Other sources of finance are either not reliable or costly. On account of organisational pattern followed by Small Scale Industries even the availability of own capital is restricted. Therefore for the growth of Small Scale Industries borrowing from financial institutions is more reliable with lower rate of interest.

## 2.7 COMPARATIVE IMPORTANCE OF SOURCES OF FINANCE :

The sources of Finance for a Small Scale Industries have changed over the years. A survey conducted in 1960 in Bombay showed the following pattern of financing of



## Small Scale Industries.

<u>AGENCY</u>	<u>PERCENTAGE</u>
Traders	66.2
Friends and Relatives	21.5
Money lenders and shroffs	3.8
Commercial Banks	1.5
Partners	1.3
Co-operative Societies	1.0
Government Agencies	0.8
Others	3.9
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All ( Total )	100.0
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( D.T.Lakalawala & J.C.Sandesara 'Small Industry  
in a big city. A survey of Bombay 1960, P. 72 )<sup>14</sup>

But the pattern of financing had changed  
drastically by 1980.

The Reserve Bank of India survey of small scale  
Industries in India in 1980 has found out that the Small  
Scale Units have<sup>15</sup>

25.7% owned capital

25.33% Corporation Loan

35.54% Bank Loan

7.4% Loan from family members

5.64% Loan from friends.

Thus while the two sources, namely, friends and relatives and money lenders have lost importance, the other two sources namely Corporation Loan and Bank Loan have gained importance. There is also a change in the percentage of Own Capital which has reduced to a great extent.

## 2.8 KARWAR TOWN :

It is the district headquarters of Uttara Kannada district of the State of Karnataka. Karwar is a natural port on the Arabian Sea Coast. It is 547 Kilometers from Bangalore, the State Capital. It is 169 kilometers away from Hubli, the nearest city. The river Kali enters the sea near Karwar. Five islands protect the port from heavy winds. Karwar has derived its name from a village called Kadwad, about 8 K.M. away from Karwar. National Highway No.17 passes through the town.

Recently a bridge has been built across the river Kali. Karwar appears to extend itself to Sadashivgad, 5 K.M. away from Karwar, after the completion of the Kali bridge.

Though Karwar is a natural port of the Arabian Sea an all-weather port of intermediate size was built and the first stage was completed only recently.

The town has a population of 47,210 as per 1981

census. Now the population has crossed 50,000/-mark. The town does not have rail-link, which is a real impediment in the growth of the town.

The Town is very near to the Goa State. The distance only about 10 Km. Fishing is the main occupation of the people here. Trade agriculture and employment are other sources of income. Very few people are in the field of industry.

The Government of India has decided to build a naval base near Karwar. It has undertaken 'Sea-bird' project about 5 Km. away from Karwar. It is going to be a very big project and the population of Karwar Town will suddenly increase to a great extent.

An atomic power generation plant is being constructed in Kaiga, which is about 30 Km. away from Karwar. The administrative office of the plant is in Karwar. The population of Karwar Town has increased considerably due to this project. The Sea-bird project and Kaiga Atomic Project have given nationwide publicity to Karwar Town.

The town is well served with commercial banks. In 1986-87 there were 11 branches of scheduled banks in Karwar. The Karnataka State Finance Corporation and The Karnataka Industrial Co-Op. Bank have opened their branches

in Karwar Town. The town has Urban Co-operative Bank and a branch of District Co-operative Bank.

There are no large industries in the town. The nearest large industry i.e. a caustic soda factory of Ballapur Industries Limited, is in Binaga, 5 Km. away.

The Small Scale Industries also have not developed well in Karwar Town. TecsoK conducted a Techno-Economic survey in 1979. The DIC started functioning in 1979. It made a list of Small Scale Industries in the District. The centre is headed by a General Manager. It has three Sub-Divisional Offices headed by Assistant Directors at Karwar Kumta and Sirsi. Though the registration of Small Scale Unit with DIC is not compulsory almost all the units in Karwar Town are registered to get the financial assistance from Banks and KSFC. The new units are registered also because they can get subsidy from the Government.

The DIC has maintained a register of Small Scale Industries in Uttar Kannada District. It encourages the establishment of Small Scale Industries in all parts of the District. The researcher has taken the registered Small Scale Industry only of Karwar Town. The total number of Small Scale Industry registered with DIC in Karwar Town is found to be 146 upto 1986-87.

The Small Scale Industries are registered

chronologically and without any further classification.

The researcher has classified, The Small Scale Units upto the Year 1986-87 as-

1. Agro based	20 units.
2. Forest based	22 "
3. Food processing	17 "
4. Engineering & repairs	58 "
5. Mining, construction	16 "
6. Miscellaneous	13 "
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Total:-	146 units
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( Source : DIC Karwar )

Agro based industries include rice and pawa mills, oil mills and flour mills.

Forest based industries include saw mills, furniture manufacturing concerns etc.

Food processing industries include bakeries, confectionaries ,condiments and soft drinks. Engineering and services industries include auto repairs, printing presses, fabrication,& Electrical services.

Miscellaneous industries include manufacturing of wax-candles, camphor, detergent cleaning powder, ink and gum etc.

The number of Small Scale Industries found in

Karwar town is not impressive. For the purpose of the study of Financing the researcher has taken a stratified random sample of 30 units out of 146 units i.e. 20 percent of the units.

Almost all of the Small Scale units in Karwar have an investment of less than Rs. 2 lakhs in plant and machinery and thus come under tiny industries sector. This is general feature in India 95 percent of the units in Small Scale Sector have investment of less than Rs. 2 lakhs. As per " Hand book of statistics on Small Scale Industries in India " issued by Development Commissioner of Small Scale Industries (DCSSI) 1985 ' average investment in plant and machinery per unit in that year ( i.e. 1985) was Rs. 47,790.

Uttar Kannada District is considered as industrially backward District. Karwar Taluka is an area identified by the Government of Karnataka as for industrial growth. The state government has recognised that Karwar is an area having potential for industrial growth. The State Government has announced 15% of the cost of fixed assets upto a maximum of Rs. 7,500/- subsidy to tiny industries coming up in Karwar Taluka.

There is no industrial estate in Karwar Town. The Small Scale units are spread throughout the town. They are not concentrated in any one place. The

Government, through the DIC has~~been~~ trying to acquire some place for the industrial estate for the last 10 years, but still it has not been able to acquire land.

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