Analysis of Remedies for Revival of Sick Small Units in Indian Economy

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Abstract

The role of small-scale industries in the economic development of India in recent years is critically analysed in this paper. Various factors affecting the growth and development of small-scale industries and the problem faced by this vital sector of Indian economy is examined. The contribution of small-scale industries in employment growth, production, export promotion and other economic indicators are discussed. Corporate failure is one of the major socio-economic problems of developing as well as developed nations. To combat this failure, it is necessary for organizations to identify revival strategies. The research paper suggests prioritization of the factors that influence the revival sick small units in India. This would help the Organisations and other players to take steps to enhance the measures of the factors, enabling these organizations to thrive. In order to combat the problem of industrial sickness, a comprehensive assessment of the magnitude of industrial sickness and an analysis of the main factors which bring about sickness are necessary. Both prevention and cure of industrial sickness would depend on our ability to identify sickness as early as possible and analyse its causes. Faulty or delayed identification would reduce the effectiveness of the remedial action such as restoring the financial viability of sick units and protecting units which would become sick. This paper examines the criteria used by official agencies in India to identify industrial sickness and points out the limitations of these criteria.

Keywords
Small-Scale Industries (SSI), Industrial, Sickness, Revival Strategies, Performance Measures

I. Introduction

India is an emerging economy with a population of more than One Billion. Nearly 40% of the population lives below the poverty line and 70% of the population is dependent on the agriculture for sustenance. The economic reconstruction of India depends on the balanced growth of economy in the fields of agriculture and industry. Because capital and finance have been scarce in India, the Government of India has encouraged alternatives to agriculture and heavy industries like small-scale industries, which can operate on limited resources. A small-scale industry can be operated by an entrepreneur without needing sophisticated machinery and modern technology. These small-scale industrial units can be established in semi-urban and rural areas where the infrastructure is underdeveloped. The objective is to use local raw material for raising production with the help of local skills. Small-scale industries provide employment without affecting the main occupation -agriculture- of illiterate people in rural areas in India. The other advantages of small-scale units are that these units need short gestation period in establishment, are less dependent on imported raw material and machinery and help in meeting a substantial part of demand of consumer goods. These units also help in solving the problem of regional disparities in economic growth (Prakash G, 1991).

In recent years, the small-scale sector in India has emerged as’ a progressive and decentralised sector on its own. Small-scale industries have made a significant contribution to employment generation in the non-agricultural sector in India. The data available from the Ministry of Small-scale Industries, Government of India (Annual Report 1999’2000) indicates that there has been an excellent growth in small scale industries in India in recent years. The number of SSI units in India has increased from 2.082 million in 1991-92 to 3.121 million in 1998 -99. The value of production in these units has increased from Rs.1786.990 Billion to Rs.5275.150 Billion in 1998-99. The volume of employment in small-scale sector has increased from 12.98 million in 1990-91 to 17.158 million in 1998-99. The growth of employment in small sector is significantly large in small sector than other organised sector in India. Small-scale industrial units have a large potential and an important role to play in India. Sickness or financial distress in small-scale sector is however of great concern to the government of India and the entrepreneurs. The number of sick units has increased from 221,472 in 1991 to 306,221 in 1999 Reserve Bank of India, (1999- 2000). The magnitude of sickness in last 9 years has prompted Reserve bank of India and the Government of India to take certain policy initiatives to eradicate sickness. The problem however still persists. The small-scale sector in India is one of the largest in the world. A study of the problems and prospects of SSI sector in India can help in understanding the problems and potentials of SMEs in emerging economies. In this paper, the current situation and future prospects of Indian small-scale industries are presented and the effects of various policy measures taken by Government of India in promoting SSI sector are examined with the objective of understanding this vital sector of Indian economy.

This paper is divided into seven sections. In section II of this paper, the legal framework relating to small-scale industries in India is explored. In section III, the macroeconomic contribution of small-scale industries to India’s economy is evaluated. In section IV, the availability of credit to SSI units from public sector banks are discussed. In section V, issues relating to sickness of the SSI units are examined. The policy issues and future prospects are analysed in section VI. Finally, an analysis of the performance of SSI sector is undertaken in Section VII and conclusions are drawn from this analysis.

A. The Indian MSME Sector: An Overview

The MSME sector is a significant contributor to the Indian economy. Based on official figures from the Ministry of MSME, November 2008, this sector contributes 8% of National GDP, comprises 50% of India’s total manufactured exports, 45% of India’s total industrial employment and 95% of all industrial units. The SME sector in India, however, has been changing over time, mostly through changes in government policy. In this section we will highlight the definition, profile, size, composition and performance of this sector.
Despite its relevance, the MSME sector has for long faced various obstacles to growth. In recognition of these difficulties and succumbing to a long sustained lobbying, the Government of India passed the MSME Development Act of 2006 which brought about major changes in this sector. The basic achievement was a clear and decisive definition of units that fall under micro, small and medium category. The definitions are based on total investment in plant and machinery for manufacturing units and investment in equipments for service units. The new definitions have expanded the plant and machinery limits and now each enterprise level includes larger investments than before. There are also allowances for smaller investments in service enterprises.

Currently, the definition used by the Ministry of Micro, Small & Medium Enterprises is described in Table 1.

Table 1: Definition of Micro, Small and Medium Enterprises

<table>
<thead>
<tr>
<th>Manufacturing Sector</th>
<th>Investment in plant &amp; machinery</th>
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<tbody>
<tr>
<td>Micro</td>
<td>Less than Rs. 2.5 million</td>
</tr>
<tr>
<td>Small</td>
<td>Rs. 2.5 to Rs. 50 million Rs. (Before 2006: 2.5 – 10 mil Rs.)</td>
</tr>
<tr>
<td>Medium</td>
<td>Rs.50 million to Rs.100 million (Not defined before 2006)</td>
</tr>
<tr>
<td>Service Sector</td>
<td>Investment in equipments</td>
</tr>
<tr>
<td>Micro</td>
<td>&lt; 1 million Rs</td>
</tr>
<tr>
<td>Small</td>
<td>1 – 20 million Rs. (Before 2006: &lt; 1 million Rs.)</td>
</tr>
<tr>
<td>Medium</td>
<td>20 – 50 million Rs. (Not defined before 2006)</td>
</tr>
</tbody>
</table>

Source: Ministry of Micro, Small & Medium Enterprises, 2007

There were no definitions for ‘medium’ manufacturing and service units until 2006. The old definition of small enterprises applied to Small Scale Industrial Undertakings (SSIs) where investment in plant & machinery was less than Rs.10 million. The old definition also applied to Small Scale Service and Business (Industry Related) Enterprises SSSBEs) where investment in fixed assets, excluding land and building was less than Rs.1 mn.

B. Industrial Sickness

The incidence of industrial sickness has been growing in India during the last decade. In India, consequent upon a number of companies falling prey to sickness, RBI has defined sickness as: “a unit is sick if it has incurred cash losses for one year and in the judgment of the financing bank, is likely to incur cash losses for current as well as for the following years, and/or there is an imbalance in the unit’s financial structure, that is when the ratio of the current assets to current liabilities is less than 1:1 and debt-equity ratio(total liabilities as a ratio of net worth is worsening” (Singh 2007). Schendel et. al (1976) initiated the attention of reason of the revival situation into the selection of right revival strategies. Arogyaswamy, Barker, and Yasai-Ardakani (1995) in an analysis of decline and revival literature view that decline and revival are strongly connected as successful revival effort have to manage together the decline and alter the firm’s strategy, and internal procedure to secure fresh resources to deal with the causes of decline.

C. Magnitude of Industrial Sickness

The incidence of sickness in the Indian economy since the 80s is clearly brought out in Table 2. The number of large sick units has increased from 241 in 1976 to 714 in 1986, while the number of sick units in the small scale sector has increased sharply from around 8 thousand to 146 thousand. Outstanding bank credit has recorded a seven-fold increase during this period. Because of the explosive growth in the number of sick units in the small scale sector, bank credit tied up in sick small scale units has recorded a yearly growth of 27.4 per cent although, during this period, outstanding credit per unit has actually decreased. Bank credit to sick units in the small scale sector has increased from less than 17 per cent in 1980 to around 27 per cent in 1986. Engineering and textiles account for more-than-half of the outstanding bank credit tied up in large sick units. Bank credit advanced to sick units in these two industries has also increased. While bank credit to large and medium industries increased from Rs 8,238 crore to Rs 19,170 crore during the period 1980-86, that to large sick units has increased from Rs 1,233 crore to Rs 3,239 crore.

D. Performance of Small Scale Enterprises (SSEs) in India

Small and medium Enterprises (SMEs) have emerged as an engine of growth in several development and developing economies of the world. In India also they have emerged as a vibrant and dynamic component of the economy by virtue of their significant contribution to GDP, industrial production and exports. Therefore, India’s GDP grew at the rate of 8.6 per cent during the period, 2003-04 to 2005-06. However, this most important contribution of this sector is towards employment generation which is second only to agriculture. The experience in recent years has shown that employment in agriculture sector has been declining, large industries have also experienced jobless growth and hence, the main responsibility for job creation rests with unorganized sector including both small and medium manufacturing and service enterprises. Considering its potential and ability, the SMEs sector has been assigned a target of 12 percent annual growth and additional employment of 4.4 million persons during Tenth Five-Year Plan. In this section, the performance of small enterprises is examined in terms of employment generation, creation of strong entrepreneurial base and its share in production and exports. The overall performance of small enterprises in India from 1991-92 to 2005-06 is presented in Table 2. The number of unit established in the year 1991-92 was 20.82 lakh and it was increased 123.42 lakh in 2005-06 which is almost six times. The figures in the above table reveals overall positive trend in the growth of number of units, output, investment, employment and exports. But the percentage of growth over the previous year (as reflected in the parenthesis of Table-2) indicates a sharp decline in the number of units in 1995-96 followed by a revival in 1996-97, then declined marginally till 1999-2000 and remained stagnant thereafter. The parentage growth of output both at current and constant prices were fluctuated over the years during the period from 1991-92 to 2005-06 which may be due to non-availability of adequate credit at the time of their capital requirement. To get adequate fund is one of the main problems for small entrepreneurs. The recent policy measures of the Government minimize the lacuna for providing credit to the small enterprise units to some extent. Employment generated by the sector was 29.49 million out of which more than 35 percent were youth in the age group 15 to 35 years. The percentage growth of employment was increased till 1994-95. It was highest in 1994-95 and thereafter it was almost stagnation which is possibly due to domestic structural reforms. But the percentage growth of exports at current prices has shown...
wide variation over the years. Export from small enterprises contributes around 35 per cent of the total export of the country. The product group where small enterprise sector dominates in export is sport goods, readymade garments, woollen garments and knitwear, plastic products, processed food and leather product. A break up of exports by important segments of small enterprises has shown some interesting facts about their share in various sectors. For instance, as much as 70 per cent of the exports of processed foods have its origin in the small-scale enterprise sector. This indeed a very encouraging sign, since it shows that small Scale enterprises (SSEs) are capable of entering and expanding in highly quality-conscious segments such as processed foods. Moreover, the growth of small food processing units has the maximum impact on poverty. Alleviation since the backward supply chain of food processing connects to the rural masses. The share of small enterprise’s export in total export of the country fluctuates in a narrow range of 31 per cent to 35 per cent since 1991-92 except in 2005-096 with the percentage share in total export went down to 29.73 per cent. It may be due to non-availability of sufficient bank credit, lack of adequate demand, acute power shortage, non-availability of sufficient raw-materials lack of modern technology etc.

Table 2: Overall Performance of Small Enterprises in India (1991-92 to 2005-06)

<table>
<thead>
<tr>
<th>Year</th>
<th>Number of Units (in Lakhs)</th>
<th>Production (Rs. Crore) (at Current Prices)</th>
<th>Employment (Nos. in Lakhs)</th>
<th>Exports (Rs. Crore at Current Prices)</th>
</tr>
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<tbody>
<tr>
<td></td>
<td></td>
<td>(at 1993-94 Prices)</td>
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<tr>
<td>1991-92</td>
<td>20.82 (7.32)</td>
<td>2,01,785 (6.42)</td>
<td>129.82 (3.28)</td>
<td>16,392 (8.46)</td>
</tr>
<tr>
<td>1992-93</td>
<td>22.46 (7.88)</td>
<td>12,35,1932 (16.55)</td>
<td>154.06 (3.58)</td>
<td>11,784 (14,784)</td>
</tr>
<tr>
<td>1993-94</td>
<td>23.88 (6.32)</td>
<td>2,71,514 (15.44)</td>
<td>139.38 (3.96)</td>
<td>25,307 (34.73)</td>
</tr>
<tr>
<td>1994-95</td>
<td>25.71 (76.6)</td>
<td>2,98,886 (23.69)</td>
<td>146.54 (5.15)</td>
<td>29,068 (14.86)</td>
</tr>
<tr>
<td>1996-97</td>
<td>28.03 (5.46)</td>
<td>4,11,858 (13.57)</td>
<td>160.00 (4.84)</td>
<td>39,248 (7.61)</td>
</tr>
<tr>
<td>1997-78</td>
<td>29.44 (5.03)</td>
<td>4,62,641 (12.33)</td>
<td>167.20 (4.50)</td>
<td>44,442 (13.23)</td>
</tr>
<tr>
<td>1998-99</td>
<td>30.80 (4.62)</td>
<td>5,20,650 (12.54)</td>
<td>171.58 (2.62)</td>
<td>48,979 (10.21)</td>
</tr>
<tr>
<td>1999-00</td>
<td>32.12 (4.29)</td>
<td>5,72,887 (10.03)</td>
<td>178.50 (4.03)</td>
<td>54,200 (10.66)</td>
</tr>
<tr>
<td>2000-01*</td>
<td>101.10 (4.1)</td>
<td>2,61,289 (11.54)</td>
<td>239.09 (4.4)</td>
<td>69,797 (28.78)</td>
</tr>
<tr>
<td>2001-02*</td>
<td>105.21 (4.1)</td>
<td>2,82,270 (7.5)</td>
<td>260.13 (4.4)</td>
<td>86,013 (20.66)</td>
</tr>
<tr>
<td>2002-03*</td>
<td>109.49 (4.1)</td>
<td>3,57,733 (14.7)</td>
<td>271.36 (4.3)</td>
<td>97,644 (13.5)</td>
</tr>
<tr>
<td>2004-05*</td>
<td>118.59 (4.1)</td>
<td>4,18,263 (16.9)</td>
<td>282.91 (4.3)</td>
<td>1,24,417 (27.4)</td>
</tr>
<tr>
<td>2005-06*</td>
<td>123.42 (4.1)</td>
<td>4,76,201 (13.9)</td>
<td>294.91 (4.3)</td>
<td>1,24,417 (27.4)</td>
</tr>
</tbody>
</table>

Notes: Figures in the brackets show percentage growth over previous year. *Figs. 2000-01 to 2005-06 include both registered and unregistered Small enterprise units and prior to 2000-01 include only registered units.

Source: Development Commissioner (SEs), Ministry of Small Enterprises, Government of India.
F. Revival Strategies

Khandwalla’s (1992), study of the revival measures lead to four broad premise under the functional areas that are found across studies- Human resource strategies, Product/market strategies, Financial strategies, Production/operations and Technology strategies.

1. Human Resource Strategies

The human resources have to actively partner with the business leadership and develop strategies to create capabilities within the organization to speed up the execution of corporate revival (Prasad, 2006). Organisations experiencing depressing development of performance generally resort to cutback as the feasible revival strategies (O’Neill 1986, Pant 1991, Smith 1995). Change in top management is another well identified human resource strategy. Leaders are frequently a contributing cause of decline (Arogyaswamy et al., 1995).

2. Financial Strategies

The objective of financial strategy is to use the financial strength of the business as an asset and to restructure the business such as reduction in the par value of shares, reduction in rates of interest, postponement of maturity of debt, conversion of debt into equity (Kumar, 2003). Studies identify financial restructuring as an essential constituent of Revival (Brown et al., 1993, DeAngelo and DeAngelo, 1990, Franks 1997, Igor 2006).

3. Marketing Strategies

Marketing is a very useful strategy for revival (Hofer 1980, Goldston, 1992). In the organisational revival literature, though a number of writers laid emphasis on the significance of marketing in the rescue of ailing organisations (Goldston, 1992, Hofer, 1980). Sales function is another key process and involves four important elements which were more apparent in the successful firms such as: 1) environmental comprehension; 2) market selection; 3) innovative market offers; and 4) managed relationships (Bibeault 1982, Finkin 1985, Harker 1998).

4. Production/Operation Strategies

Hofer(1980) in a study of twelve cases of badly performing organizations, where he found for operating problems the solution is operating remedies and for strategic problems, strategic remedies. Thus, organisations that are failing due to operational causes opt for operational revival strategies and strategic causes opt for strategic revival strategies and rarely were operational failure addressed with strategic revival actions (Hambrick and Schecter, 1983).

5. Corporate Planning Strategy

Contraction and consolidation strategies for revival are implemented when a corporation’s predicament are not all-inclusive (Pearce and Robinson, 1992). Corporate reorganization is a different revival strategy which frequently engages refocusing or eliminating non-core businesses. (Beixin et al 2008).

II. Analysis of Policies and Performance

The performance of SSI sector in India can be analysed based on the economic rationale for intervention by the governments in support of small and medium scale enterprises developed by The World Bank and discussed in the paper by Hallberg (2000). According to Hallberg (2000), the economic importance of SMEs can be investigated based on a number of factors such as share of firms and employment, labour intensity of SMEs, efficiency and social, political and equity justifications. The first criterion discussed by Hallberg (2000) is the share of firms and employment. From the data given in Tables 1, 2, 3 it is observed that the SSI sector in India has shown considerable growth from 1990-91 in terms of number of units, employment numbers, production and exports. Nearly 40% of India’s G.D.P. is contributed by SSI sector. Although the employment numbers in this sector of economy could be high compared to production levels this could be explained as being due to the nature of product composition in India, as suggested by Hallberg (2000). The reservation policy of the Government of India in regard to production of consumer goods in small scale sector could possibly contribute to large labour force working in SSI sector in India. Nearly 812 items of consumer goods are reserved for exclusive manufacturing by SSI sector and large labour force could be working in these sectors.

Hallberg (2000) further suggests that “small firms have ‘higher job creation and destruction rates than large enterprises and may offer lesser job security than large firms.” In India the destruction rate of SSI firms is close to 9-10% and revival rate of SSI units is very small (only 6-7% of the sick units are revived). This data supports the contention of Hallberg(2000) in regard to destruction of small firms. Another important issue in regard to SSI units is the efficiency of these units. According to Hallberg (2000), “smallest firms are least efficient”. This view of Hallberg (2000): is supported by Goldar (1988) in regard to SSI sector in India. According to Goldar (1988),”while small Indian modern sector firms are more labour intensive than larger firms they are less efficient”. Given the suggestions of Hallberg (2000) and Goldar (1988), it may therefore be more appropriate to compare the relative efficiency of SSI units in India over a period of time instead of comparing their efficiency with larger firms in India.

III. Conclusion

The major strategies we found from our study for revival are Employee engagement, Aggressive promotion of old products in new market, Cost management strategies, Investments in new markets and R&D, Focus on core business, Changes in product mix and pricing, Lean management, Image building The successful organisations has higher scores on many strategy factors, especially the ones contributing to organisation development such as employee engagement, cost management, focus on core business and lean management. The factor were there are no significant differences are focus on core business, changes in product mix and pricing, and investments in new markets and R&D, which implies that these strategies are equally used by both the groups. While these are functional strategies the problem with the unsuccessful group may be that they failed to build the organisation through the strategies mentioned above as characteristic of the successful group. Besides, the unsuccessful group had also tried to aggressively promote old products in new markets where they have a significantly higher score. Lean management as a strategy was used more frequently by successful revival than the unsuccessful revival. There was a difference in the investment strategies, which was significantly different for the successful revival. Cost management was more frequently used in successful revival. It was found that revival strategies of successful and unsuccessful were different to a certain extent. There have also been strategies which are common for successful and unsuccessful organizations. Thus, it is possible that different kinds of revival strategies are needed for successful and unsuccessful organisations.
“GLOBALIZATION WILL KILL SMALL-SCALE INDUSTRIES IN INDIA”– Globalization is the metamorphosis of the individual nations into an integrated entity by means of their interconnection on an economic, social and cultural level, fuelled by easy transport and communication among them. It is the modern renaissance that makes ideas, goods, services, trade, technology and culture permeate into the entire geography of the world thus turning it into a global village. While globalization is a large scale phenomenon, small scale enterprises are a local phenomenon but having effects of dimensions as large as it’s global ‘friend and foe’. Friend– because both globalization and small scale industries are the two wheels of the vehicle of economic growth and prosperity; foe– because some argue that given the developing nation that India is, Small Scale Industries (SSIs) can suffer and strangulate to death by the fierce competition put up by globalization. Let us observe and decide.

Small scale industries in India are facing great threats and competition due to liberalized policies. The robust and vibrant small scale industries sector (now MSE) can derive the benefits of the new opportunities provided by the supporting policies which aim not only to protect but also to promote this segment. The step towards dereservation by the government is definitely a positive step as it has not proved to benefit much. The inclusion of service sector is indeed a good initiative to have new schemes to promote this sector.

IV. Recommendations
• The State as well as Central Government should provide necessary facilities to face cut throat competition.
• To provide continuous power supply to units for smooth flow of production.
• To provide proper training inputs from professional institute.
• To prevention of industrial sickness and revival of viable sick units.
• To provide infrastructure facilities to units.
• There is a need to promote professionalism in units.
• It is need to adopt total quality management in units.
• The SSI units should adopt ISO standards.
• The foreign direct investments should be allowed.
• The industrial policy should in favour of SSI unit.
• The political intervention in the process needs to be unveiled completely.
• The focus should be on providing backward and forward linkages.
• The strengthening the SSI units through promotion of quality competitiveness and research and development.
• The streamlining procedures, bottlenecking and creation of hassle free industry friendly environment.
• The commercial exploitation of local resources and economic potential.
• The innovation and learning mechanism and important breakthroughs can take place in the SSI sector for its survival and growth.
• The SSI units to look upon the employees as an assets and take cognition of the need to improve their skill.

References