

# Financial Performance Evaluation of Small Scale Industries: Impact and Issues

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## Abstract

*Small scale industries either are known as SSI or generally as the Small and Medium enterprises refer to those small entrepreneurs who are engaged in production, manufacturing or service at a micro scale. Small scale industries constitute the backbone of a developing economy with its effective, efficient, flexible and innovative entrepreneurial spirit. Round the world SSI units have been accepted originator of economic growth and for promoting equitable development. The contribution of SSIs to the Indian economy in terms of employment generation, reducing regional imbalances. Accounting and financial evaluation have always been seen as the best route to a successful business career as it is considered as the language and basic tool of a business organization which helps to determine how a business is doing. The growth of the small-scale enterprises can be determined through maintenance of proper records of accounts, which provides the basis for safeguarding and controlling the business properties. We found that there are many perceived factors affecting their adoption of accounting practices and their effects on their business operations in the area. Among such factors include; lack of adequate training, willful misconduct, and negligence. This article presents an empirical investigation of financial performance evaluation practiced by SSIs and its impact.*

**Keywords:** SSI, performance evaluation, average growth, Challenges

## INTRODUCTION

Small-scale industries have played a very important role in the development of country. The government in its budget normally emphasizes on the contribution of the small and medium scale enterprises. The role of small-scale industries has always been supported in a country like India with various opinions such as employment, equality, latent resource, trickling effect, insurance against social tension, distributive effect, creation of social eco system and decentralization etc. The other arguments in favor of small-scale industries are making provision for self-employment and capital formation and they are skill light, import light and quick yielding. Analysis of the data on SSIs has received different responses from different economists in different studies, right from one of the earliest studies in 1961. The performance of the small-scale sector has a direct impact on the growth of the overall economy. The performance of the small scale sector in terms of parameters like number of units, production, employment and exports will help to understand its role in the economic development of the country.

Small-Scale Industries and Economic Development of India

### *Employment Generation*

The basic problem that the Indian economy is confronting is increasing pressure of population on the land and the need to create massive employment opportunities. This problem is solved to a large extent by SSIs because SSIs are labor-intensive in nature. They generate large number of employment opportunities. Employment generation by this sector has shown a phenomenal growth. It is a powerful tool of job creation.

Mobilization of Resources and Entrepreneurial Skill

SSIs can mobilize a good amount of savings and entrepreneurial skill from rural and semi-urban areas which remain untouched from the clutches of large industries and put them into productive use by investing in small-scale units. Small entrepreneurs also improve social welfare of a country by harnessing dormant, previously overlooked talent. Thus, a huge amount of latent resources is being mobilized by the small-scale sector for the development of the economy.

### ***Equitable Distribution of Income***

The SSIs ensure equitable distribution of income and wealth in the Indian society which is largely characterized by more concentration of income and wealth in the organized sector keeping unorganized sector undeveloped. This is mainly due to the fact that small industries are widespread as compared to large industries and have large employment potential.

### ***Regional Dispersal of Industries***

There has been massive concentration of industries in a few large cities of different states of India. People migrate from rural and semi-urban areas to these highly developed centers in search of employment and sometimes to earn a better living which ultimately leads to many evil consequences like overcrowding, pollution, creation of slums, etc. This problem of Indian economy is better solved by SSIs which utilize local resources and bring about dispersion of industries in various parts of the country thereby promoting balanced regional development.

SSIs have registered a phenomenal growth in export over the years. The value of exports of products of SSIs has increased from ` 6979.7 million in 2000-01 to ` 28,384.7 million in 2011-12. Thus they help in increasing the country's foreign exchange reserves thereby reducing the pressure on country's balance of payments.

### ***Role and Importance of Small Scale Industries***

Small scale industries are important because it helps in increasing employment and economic development of India. It improves the growth of the country by increasing urban and rural growth. Role of Small and medium scale enterprises are to help the government in increasing infrastructures and manufacturing industries, reducing issues like pollution, slums, poverty, and many development acts. Small scale manufacturing industries and cottage industries play a very important role in the economic development of India. If any amount of capital is invested in small scale industries it will help in reducing unemployment in India and increasing self-employment. The industry is a sector in which the production of goods is a segment of the economy. Let us learn more about the importance of Small scale industries and how SSI helps in developing the country.

### ***Small Scale Industries:***

Previously, the definition of small scale industries depended upon the business's capital and labor. This definition is still used to demarcate between small, medium and large-scale industries.

The Central Government has the authority to determine capital investment requirements for small-scale industries. These requirements are listed under the Industries (Development and Regulation) Act, 1951.

A small enterprise in which investment in plant & machinery ranges between Rs. 25 lakhs to Rs. 5 cores is a small-scale industry.

Similarly, for industries that provide services, the investment requirement is between Rs. 10 lakhs and Rs. 2 cores.

Every small-scale industry plays a big role in the Indian economy. Apart from providing employment to cores of people, it has the added benefit of minimum capital requirements. The government also offers several tax benefits to SSI for this purpose.

Furthermore, they can exist in urban as well as rural areas. Small Scale Industries have been able to compete with large-scale industries and multinational corporations because of this. Due to reasons like these, they are of great importance.

***Roles that SSIs play in the Indian economy:***

***1. SSI Increases Production***

India is one of the world's fastest growing economies in the world. Consequently, its production output is massive. It is pertinent to note that SSIs contribute almost 40% of India's gross industrial value. These industries produce goods and services worth over Rs. 40 lakhs for every investment of Rs. 10 lakhs. Furthermore, the value addition in this output increases by over 10%. Here is another interesting statistic about Small scale industries. The number of Small Scale Industries in India increased from around 8 lakhs in 1980 to over 30 lakhs in 2000. This figure has grown even more in recent years owing to the government's 'Ease of Doing Business' policies. As a result of this, the total industrial production output rose tremendously in the last few years. SSIs are, therefore, strongly responsible for the growth of India's economy.

***2. SSI Increases Export***

Apart from producing more goods and services, SSIs have been able to export them in large numbers as well. Almost half of India's total exports these days come from small-scale businesses. 35% of the total exports account for direct exports by SSIs, while indirect exports amount to 15%. Even trading houses and merchants help SSIs export their goods and services to foreign countries.

***3. SSI Improves Employment Rate***

It is important to note firstly that Small Scale Industries employ more people than all industries after agriculture. Almost four persons can get full employment if Rs. 10 lakhs are invested in fixed assets of small-scale sectors. Furthermore, SSIs employ people in urban as well as rural areas. Consequently, this distributes employment patterns in all parts of the country and prevents unemployment crisis.

***4. SSI Open New Opportunities***

Small-scale industries offer several advantages and opportunities for investments. For example; they receive many tax benefits and rebates from the government. The opportunity to earn profits from SSIs are big due to many reasons. Firstly, SSIs are less capital intensive. They even receive financial support and funding easily. Secondly, procuring manpower and raw materials is also relatively easier for them. Even the government's export policies favour them heavily.

***5. SSI Advances Welfare***

Apart from providing profitable opportunities, Small Scale Industries play a large role in advancing welfare measures in the Indian economy as well. A large number of poor and marginalized sections of the population depend on them for their sustenance. These industries not only reduce poverty and income inequality but they also raise standards of living of poor people. Furthermore, they enable people to make a living with dignity.

***10 Major Problems faced by the Small Scale Industries of India***

This sector can stimulate economic activity and is entrusted with the responsibility of realizing various objectives generation of more employment opportunities with less investment, reducing regional imbalances etc. Small scale industries are not in a position to play their role effectively due to various constraints. The various constraints, the various problems faced by small scale industries are as under:

***(1) Finance:***

Finance is one of the most important problem confronting small scale industries Finance is the life blood of an organisation and no organisation can function properly in the absence of adequate funds. The scarcity of capital and inadequate availability of credit facilities are the major causes of this problem. Firstly, adequate funds are not available and secondly, entrepreneurs due to weak economic base, have lower credit worthiness. Neither they are having their own resources nor are others prepared to lend them. Entrepreneurs are forced to borrow money from money lenders at exorbitant rate of interest and this upsets all their calculations. After nationalization, banks have started financing this sector. These enterprises are still struggling with the problem of inadequate availability of high

cost funds. These enterprises are promoting various social objectives and in order to facilitate then working adequate credit on easier terms and conditions must be provided to them.

**(2) Raw Material:**

Small scale industries normally tap local sources for meeting raw material requirements. These units have to face numerous problems like availability of inadequate quantity, poor quality and even supply of raw material is not on regular basis. All these factors adversely affect the functioning of these units. Large scale units, because of more resources, normally corner whatever raw material that is available in the open market. Small scale units are thus forced to purchase the same raw material from the open market at very high prices. It will lead to increase in the cost of production thereby making their functioning unviable.

**(3) Idle Capacity:**

There is under utilization of installed capacity to the extent of 40 to 50 percent in case of small scale industries. Various causes of this under-utilisation are shortage of raw material problem associated with funds and even availability of power. Small scale units are not fully equipped to overcome all these problems as is the case with the rivals in the large scale sector.

**(4) Technology:**

Small scale entrepreneurs are not fully exposed to the latest technology. Moreover, they lack requisite resources to update or modernise their plant and machinery. Due to obsolete methods of production, they are confronted with the problems of less production in inferior quality and that too at higher cost. They are in no position to compete with their better equipped rivals operating modern large scale units.

**(5) Marketing:**

These small scale units are also exposed to marketing problems. They are not in a position to get first hand information about the market i.e. about the competition, taste, liking, disliking of the consumers and prevalent fashion.

With the result they are not in a position to upgrade their products keeping in mind market requirements. They are producing less of inferior quality and that too at higher costs. Therefore, in competition with better equipped large scale units they are placed in a relatively disadvantageous position. In order to safeguard the interests of small scale enterprises the Government of India has reserved certain items for exclusive production in the small scale sector. Various government agencies like Trade Fair Authority of India, State Trading Corporation and the National Small Industries Corporation are extending helping hand to small scale sector in selling its products both in the domestic and export markets.

**(6) Infrastructure:**

Infrastructure aspects adversely affect the functioning of small scale units. There is inadequate availability of transportation, communication, power and other facilities in the backward areas. Entrepreneurs are faced with the problem of getting power connections and even when they are lucky enough to get these they are exposed to unscheduled long power cuts.

Inadequate and inappropriate transportation and communication network will make the working of various units all the more difficult. All these factors are going to adversely affect the quantity, quality and production schedule of the enterprises operating in these areas. Thus their operations will become uneconomical and unviable.

**(7) Under Utilization of Capacity:**

Most of the small-scale units are working below full potentials or there is gross underutilization of capacities. Large scale units are working for 24 hours a day i.e. in three shifts of 8 hours each and are thus making best possible use of their machinery and equipment.

On the other hand small scale units are making only 40 to 50 percent use of their installed capacities. Various reasons attributed to this gross under- utilisation of capacities are problems of finance, raw material, power and underdeveloped markets for their products.

**(8) Project Planning:**

Another important problem faced by small scale entrepreneurs is poor project planning. These entrepreneurs do not attach much significance to viability studies i.e. both technical and economical and plunge into entrepreneurial activity out of mere enthusiasm and excitement. They do not bother to study the demand aspect, marketing problems, and sources of raw materials and even availability of proper infrastructure before starting their enterprises. Project feasibility analysis covering all these aspects in addition to technical and financial viability of the projects, is not at all given due weight-age.

**(9) Skilled Manpower:**

A small scale unit located in a remote backward area may not have problem with respect to unskilled workers, but skilled workers are not available there. The reason is Firstly, skilled workers may be reluctant to work in these areas and secondly, the enterprise may not afford to pay the wages and other facilities demanded by these workers. Besides non-availability entrepreneurs are confronted with various other problems like absenteeism, high labor turnover indiscipline, strike etc. These labor related problems result in lower productivity, deterioration of quality, increase in wastages, and rise in other overhead costs and finally adverse impact on the profitability of these small scale units.

**(10) Managerial:**

Managerial inadequacies pose another serious problem for small scale units. Modern business demands vision, knowledge, skill, aptitude and whole hearted devotion. Competence of the entrepreneur is vital for the success of any venture. An entrepreneur is a pivot around whom the entire enterprise revolves. Many small scale units have turned sick due to lack of managerial competence on the part of entrepreneurs. An entrepreneur who is required to undergo training and counseling for developing his managerial skills will add to the problems of entrepreneurs. The small scale entrepreneurs have to encounter numerous problems relating to overdependence on institutional agencies for funds and consultancy services, lack of credit-worthiness, education, training, lower profitability and host of marketing and other problems. The Government of India has initiated various schemes aimed at improving the overall functioning of these units.

**Conclusion:**

Effective management requires leadership plus administrative skills in planning, organizing, directing and controlling the entire business operations. Because of limited financial resources and inability to hire professional managerial personal, small-scale units lack specialization in the execution of various functions of management. The majority of small-scale units are sole proprietorship organization and as such these units are highly personal in nature, i.e., the single man's show. It is very difficult to take quick decisions in all respects and implementing these decisions promptly since the sole proprietor is neither a production oriented engineer nor sales oriented merchant. He has no time to look after other functions. Moreover, the majorities of sole proprietors is illiterate or have low level of education and lack managerial skill.

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