©KY PUBLICATIONS
RESEARCH ARTICLE
Vol.2.Issue.2.2015

IJBMAS
E ISSN 2349-4638

http://www.ijbmas.in
INTERNATIONAL JOURNAL OF BUSINESS, MANAGEMENT AND ALLIED SCIENCES (IJBMAS)
A Peer Reviewed International Research Journal

A SUSTAINABLE STUDY ON SICKNESS OF SMALL SCALE INDUSTRIAL ENTERPRISES

Dr.T.SREEKRISHNA[1], A.HARI PRASAD[2*]

[1]Associate Professor, Department Of Management Sciences in R.V.R & JC College of Engineering, Guntur, Andhra Pradesh, India.

[2]*Ph.D Research Scholar, Department of Business Management, Acharya Nagarjuna University, Nagarjuna Sagar, Guntur District, Andhra Pradesh

E-mail: [1]hariprasad.avula99@gmail.com [2]t.sreekrishna@gmail.com

ABSTRACT

Sickness[i] in industrial units is a gradual process and does not develop suddenly. In the initial stages, it gets reflected in the form of defects and mistakes in the unit's functional areas like production, finance and management. Later it is observed in the form of symptoms like irregular or unsatisfactory turnover in the account, slow and unsatisfactory movement of stocks, decline in production, sales and profitability, frequent violation of terms and condition and asking for additional grants.

The other common problems faced by SSI[ii] towards of creation of excess capacity: Absence of comprehensive data. Under-utilization of installed capacity. Inadequate planning production. Persistent recessionary condition. Shortage of raw material.

Article Info:
Article Received on:02/06/2015
Article Revised on:17/06/2015
Article Accepted on:20/06/2015

1. INDUSTRIAL SICKNESS

Industrial sickness is a significant problem in many market economies. in the Indian private sector, it has been estimated that currently over 450 large manufacturing units end over 125,000 small units are sick, with more than rupees four thousand crores (over $3 billion) of the funds of financial institutions and banks tied up in these sick units. In India, the amount of funds of financial institutions tied up in defaulting accounts may be growing at over 10% per annum, and therefore, may double every seven years.

In India and elsewhere in the Third World, the problem of sickness is likely to grow worse. The number of new units coming up in India every year has grown over ten times since independence – to some 60,000 registered new manufacturing units a year, thanks to various incentives offered by the government, the financial support provided by the apex and state level financial institutions, and the facilities provided in industrial estates. The percentage of entrepreneurs receiving any sort of training in setting up and managing units is miniscule. Inadequate capacity to manage units may mean more and more units turning sick. Besides, literalisation of the economy is likely to accelerate the pace of entrepreneurship.

A Reserve Bank of India study indicated that 84% of sick large firms for which viability studies were conducted were considered to be potentially viable, though only about 10% of the small units were so considered.

The sick[iii] industrial companies (special provision) Act 1985 identifies sickness in terms of cash losses for two consecutive financial years and accumulated losses equaling or exceeding the net worth of the company at the end of the second financial year.

The identification of sick SSI units has been modified as under: "A small-scale industrial unit should be considered as sick if it has, at the end of any accounting year, accumulated losses equal to or exceeding 50 percent of its peak net worth in the immediately preceding five accounting years" (Bihar Chambers of Commerce, Sep. 1989).

The Reserve Bank of India considers a unit as sick if it has incurred a cash loss for a year and is likely to incur a cash loss in the current and coming years, along with a poor financial structure (current ratio less than 1:1, worsening debt-equity ratio). The Indian term lending financial institutions tend to consider a unit as sick if it has consecutively defaulted for four half-yearly loan and interest installments due to the financial institutions, has made cash losses for two consecutive years, or has lost its net worth by 60%, and has mounting arrears of statutory and other liabilities. Bidani and Mitra compare corporate sickness with bodily sickness, and indicate that abnormal functioning of a unit or any of its areas of management (production, marketing, finance, personnel or general management) would amount to corporate sickness.

A unit is sick if its financial performance is well below its performance potential. An operational way of judging this is to compare the unit's current financial performance with its performance in the past during comparable business conditions, and to compare its current performance with other comparable units in the industry known to be efficiently managed. These two comparisons should provide a rough indication of how far the units is operating below its performance potential. Thus, a unit may be considered sick if it is operating way below its or defaulting) and the prospects are that it will continue to operate below its performance potential.

2. Reasons of Industrial Sickness

Units[iv] satisfying one or more of the above criteria were treated by enumerators as not being run satisfactorily and the reasons for the same were elicited. Table II indicates the reasons as given by the units suffering from sickness/ incipient sickness. Lack of demand and shortage of working capital are the main reasons for sickness/incipient sickness in the SSI sector.

TABLE II

Reason for Sickness/incipient Sickness in SSI Sector

Reason for sickness/ incipient sickness	Percent of sickness/incipient sick units*	
	Registered SSI sector	Unregistered SSI sector
Lack of demand	71.6	84.1
Shortage of working capital	48.0	47.1
Non-availability of raw material	15.1	15.2
Power shortage	21.4	14.8
Labour problems	7.4	5.1
Marketing problems	44.5	41.2
Equipment problems	10.6	12.9
Management problems	5.5	5.1

**These units include village industries as well*

The states of Kerala, Karnataka, Chandigarh (UT), Maharashtra and Tamil Nadu had the maximum share of sick units in the registered SSI sector.

As per the data compiled by the Reserve Bank of India from the scheduled commercial banks, the sickness in the small-scale industries has decreased in the recent years. The number of sick small-scale industries from March 2007 to March 2013 is given in Table III.

TABLE III

Sickness in SSI Sector

As at the end of	Total sick units		Potentially viable	
	Number*	Amount outstanding (Rs crore)	Number*	Amount outstanding (Rs crore)
March 2007	235,032	3,609.20	16,220	470.31
March 2008	221,536	3,856.64	18,686	455.98
March 2009	306,221	4,313.48	18,692	376.96
March 2010	304,235	4,608.43	14,373	369.45
March 2011	249,630	4,505.54	13,076	399.17
March 2012	177,336	4,818.92	4,493	416.39
March 2013	167,980	5,706.35	3,626	624.71

**These units include village industries as well*

As a follow-up to the measures announced by the government in the Comprehensive Policy Package for the SSIs on August 30, 2000, the Reserve Bank of India constituted a working group under the chairmanship of the then chairman, Indian Bank Association, Mumbai, to review the existing guidelines and recommend the revision of guidelines, making them transparent and non-discretionary for the rehabilitation of currently sick and potentially viable SSI units. The working group has submitted its report to RBI.

All the major recommendations of the working group have been accepted by the RBI including a change in the definition of sick SSI units, norms for deciding on the viability of sick units, etc. The revised definition would enable banks to take action at an early stage for revival of the units.

Based on the accepted recommendations of the working group, RBI drew up the revised guidelines for rehabilitation of sick SSI units, which were circulated to the banks on January 16, 2002 for implementation.

A view of industrial sickness is useful for many reasons.

I) There is no confusion between sickness and poor performance beyond the control of the unit. After all, a unit may be making cash losses because the industry it is in is in a deep recession, not because of poor management. In such a case the industry is sick, not the unit, and any revival actions need to be industry-oriented rather than unit-oriented.

II) Revival efforts are likely to yield good dividends when the unit is performing well below its potential, as several case studies have shown.

III) Identification of relatively poor performance can cue a unit or the financial institutions to earlier revival efforts than waiting for the unit to make losses – and the earlier the revival efforts, the faster, more effective, and less expensive may be the turnaround.

IV) From a social viewpoint, the closer enterprises operate to their performance potential the better generally would be resource utilisation, and so any efforts of stakeholders (including the management, the government, and the financial institutions) to keep enterprises operating at or near their performance potential should yield good dividends for the economy.

3. Western Work on Industrial Sickness in Indian content

1. Most studies agree that sickness can be caused by a wide variety of factors. Thereby, sickness can be caused by factors internal to the organisation, such as inadequate management or a sub-optimal plant, and/or by factors external to the organisation, such as increased competitive pressure, recession, or strike. Table 1.1 summarises the causes as identified in a number of studies.

2. The major cause of industrial sickness seems to be poor quality of top management. This may take one of several forms: concessive conservatism, excessive complacency, growth mania, poor financial control, excessive centralization and authoritarianism, weak board and weak watch-dog function, excessive commitment to policies that worked well once but are no longer appropriate, poor financial or marketing management, etc. (see Table 1.1). Although such contextual factors as price competition and recession are significant causes, these are more often than not contributory factors rather than main factors. In an American study it was found that external factors (slumps, exchange rate changes, credit squeezes, inflation, etc.) may have been mainly responsible for only about 10% of corporate declines. On the other hand internal causes of decline, such as one man rule, lack of management depth, management succession problems, inbred, bureaucratic management, weak financial control, unbalanced top management, a weak board, etc., accounted for about 70% of declines (the remaining 20% declines were caused by a mix of external and internal factors). As a British researcher put it, "……. a crisis situation is likely to occur most frequently when a firm, already weakened by poor management, lack of control and inefficiency, is subject to adverse movements in market demand and commodity prices, price competition and ….. problems resulting from the so-called big project".
   The two vital errors of omission on the part of management may be failure to respond adequately to market place changes, and inadequate control of operations. Some significant errors of commission seem to be overexpansion and excessive leverage (i.e. debt).
3. Many declines tend to take place during organisational transitions. For instance, once an entrepreneurial venture has been established, the failure to induct a professional manager to set up appropriate financial control, production planning, etc., systems may lead to sickness; if a professional manager is hired, and the organisation grows, excessive centralisation may lead to sickness; if decentralisation does take place, accompanied by a sound management control system, the resulting depersonalisation may cause sickness unless the management communicates some core values to the rank and file that act as a binding force.
4. Organizational size, and the bureaucratisation of the organisation a growth in size often implies, may be an important cause of sickness. Large size implies growing reliance on rules and regulations, hierarchy, and specialisation of functions. These, in turn, can lead to staff alienation, distorted communications, administrative rigidity, inter-departmental conflicts, and sub-optimisation, and result in organizational sickness.
5. The major causes of sickness are not necessarily the major inhibitors of revival. For instance, in a British study of 40 turnaround cases, the four major causes of sickness were found to be lack of financial control on the part of management, an inadequate chief executive, price competition, and operating inefficiency. However, of the four, only price recovery. In other words, not only was price competition a common cause of sickness, the chances of recovery of units falling sick because of competition tended to be slim. Three other major inhibitors of recovery of units falling sick because of inhibitors of recovery were a sub-optimal plant, high overheads, and weak marketing. Thus, the more of these four factors are present in a sickness situation, the less salvageable may the unit be. On the other hand, though poor financial control, an inappropriate chief executive, and operating inefficiency may be major causes of sickness, they seem to be far easier to remedy, and, therefore, they do not render a unit unsalvageable.
6. Western experts have suggested that for revival purposes it may be useful to consider three types of sickness situations. The first is the hopeless case. The hopeless case is characterised by such factors as a severe decline in the unit's core business area; a single product, single plant operation that makes divestiture difficult; and relatively high fixed costs in relation to value added, which makes the unit highly vulnerable to even modest business declines. The second suggested category is that of short-term survivors, who can break even for a while but have no long-term competitive advantage, and therefore, may survive in a boom but are likely to go under in a recession. The third category consists of those with potential for sustainable recovery because of a good product or process base but sickness due primarily to poor management. Obviously, the clear policy implication for financial

institutions would be to stop further assistance to the hopeless cases and give full but conditional assistance to those with potential for sustainable recovery, with some ambiguity about what to do vis-à-vis the short-term survivors. The earlier (and better) the diagnosis the lower may be the costs of effective action.

Internal Causes

1. Inadequate management. Excessively cautions, bureaucratic permissive, or authoritarian management. Weak board and watchdog function. Lack of management depth.
2. Unprofitable acquisitions, expansions, poor choice of plant of technology. Growth mania. Neglect of core business in the drive for diversification. Poor post – acquisition management.
3. Lack of financial control and proper accounting information. Inability to pinpoint which products and customers are profit yielding, which loss making.
4. Poor marketing and distribution. Poorly motivated or trained sales force. Ineffective advertising and promotion. Poor after sales service. Lack of focus on key products and customers. No new product development.
5. Overtrading; inadequate working capital to finance sales growth. Proliferation of low margin or loss making sales.
6. Poor financial policies – excessive leverage, low profit retention for reinvestment, short term borrowing for long term needs, etc.
7. Big projects with long gestation periods, start-up difficulties, poor timing, under-estimated costs and over-estimated returns, high market entry costs.
8. The unresposiveness of the firm to market and technological changes.
9. High unit costs relative to competitors due to unfamiliarity with business, or inability to take advantage of economies of scale, or lower market share or vertical integration compared to rivals, or government – imposed pollution control, social welfare, or other costs, or high overheads because of technology or plant choice, etc.

External Causes

10. Increased competitive pressure on the firm.
11. Decline of market demand.
12. Adverse movement in input prices and interest rates, combined with price stagnation or decline in marketed products.
13. Strikes.

4. PREVENTION OF SICKNESS

Prevention of Sickness by Owners and Management

The primary responsibility for preventing sickness lies with the owners and management of the organisation. Owners and management are not always identical, however, although they tend to be identical for small and medium sized units. In widely held larger companies, in subsidiaries of multinationals, in companies belonging to business houses, and in government owned enterprises there can be a substantial separation between ownership and management. In such companies, where the management is competent and honest, the primary responsibility for prevention rests with the management. Where it is incompetent or dishonest (these are the primary causes of sickness) the primary responsibility rests with owners.

As far as sickness prevention is concerned, the essentials are obvious: competent management of various functions like general management, marketing, operations, personnel, and finance; and a good performance reporting system designed to provide top management/owners timely information on critical parameters such as sales, production, profits, cost variance, profit variance, etc[v].

Prevention of Sickness by Government

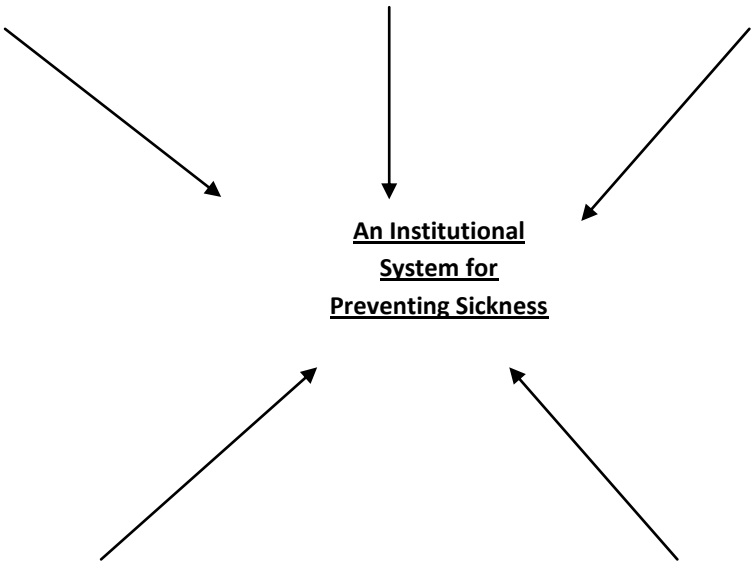
In the Third World, the government is often a dominant stakeholder even in privately owned enterprises. The various tax reliefs and subsidies it provides, its ownership or control of the institutions that finance organisations, its enterprises related policies stemming from its overriding concern with industrial development, etc., make it a major stakeholder even in minor enterprises. Its actions often affect the health of whole enterprises. Like magic new industries arise though appropriate policies, tax incentives, subsidies,

infrastructural facilities, etc., and like magic they disappear also, or get sick. The policies and financial and infrastructural support provided – or withheld – by the government is an important determinant of health and sickness. Frequent changes in government policies need to be avoided to reduce industrial sickness[vi].

Table 1.1: CAUSES of SICKNESS

EXHIBIT – A MODEL INSTITUTIONAL SYSTEM FOR PREVENTING SICKNESS

Continuous Monitoring of Unit	Careful Project Appraisal	Professional Institutional response to Unit's Problems
Periodic financial reports Desk officer for client unit	Independent verification of sales, profits, etc., projections of the client	Training of desk officers and deputed advisers in professional industrial and financial management
Institutional nominee(s) on the board Periodic inspections	Careful scrutiny of technology and plant size choices, location, government-related contingencies, and quality of management	Discretionary authority to monitoring desk officer to commit the institutions (up to some limits) to immediate contingency reliefs
Institutional adviser deputed to unit, especially to monitor project implementation in "risky" ventures	Use of external consultants for appraising large or "risky" projects	Better co-ordinations and faster response by financial institutions through a smaller consortium
Inter-institutional reviews of unit		
Market intelligence and industry cells		Lead agency concept



Required systems at client units	Incentives to units to remain healthy
Approval of financial institutions for appointing (or removing) internal and statutory auditors, etc.	Interest relief if no sickness
Professional management training for promoters	Penal interest for avoidable project cost escalations, careless or false sales and profit projections

5. Rehabilitation of Sick Units

Growing incidence[vii] of sickness of SSIs is yet another area of concern. Mortality of SSI unit has been showing an increasing trend because of internal and external factors including international competitive environment. This has wider implications including the locking up of funds of the lending institutions, loss of scarce material resources, and a large number of workers and other employees becoming jobless.

With a view to ensuring that potentially viable sick SSI units are provided with timely and adequate assistance by all agencies concerned, there are State Level Inter-Institutional Committees (SLIICs) involving State Government, Financial Institutions, Commercial Banks and SIDBI. SSI associations are also represented on these committees. A sub-committee of the SLIIC has also been set up in each state to examine the individual cases referred to it for rehabilitation. It is suggested that the SLIIC may be given statutory backing to ensure its effectiveness. To arrest the incidence of growing sickness, the RBI has issued a complete set of revised guidelines to commercial banks in January 2002, which supersedes the guidelines issued in 1993, on the basis of the recommendations of the Working Group constituted for the purpose.

The major change from the earlier guidelines relates to revision in the definition of a Sick SSI unit. This is based on the recommendation of the S.L.Kapur Committee Report on Credit to SSI of 1998, and the Report of the Working Group on Rehabilitation of Sick SSI Units constituted by RBI of 2001. The revised definition of a Sick SSI unit adopted in the guidelines is as follows:

- An SSI unit is declared sick if any of its borrowal accounts remains sub-standard for more than six months, i.e. principal or interest, in respect of any of its borrowal accounts has remained overdue for a period exceeding one year; or
- There is erosion in the net worth due to accumulated cash losses to the extent of 50 per cent of its peak net worth during the previous accounting year; and
- The unit has been in commercial production for at least two years.
- The non-performing period of the account in respect of Sick SSI units has thus been reduced from 2 ½ years to one year. The requirements of overdue period exceeding one year will remain unchanged even if the present of classification of an account as sub-standard is reduced in due course.

The guidelines also cover aspects relating to monitoring, viability, incipient sickness, relief and concessions that can be extended by banks. The revised criteria will enable banks to detect sickness at an early stage, and facilitate corrective action for the revival of the unit. The revised guidelines also stipulate that the rehabilitation package should be fully implemented within six months from the date of the unit is declared potentially viable/viable. During this interim period, banks/financial institutions are required to do 'holding operation' allowing the sick unit to draw funds from the cash credit account, up to the extent of the deposited sale proceeds. The RBI package should be supplemented by a package from the State Governments.

6. Marketing Sickness

The marketing[viii] is the major area of operation in SSI sector, which is neglected in many cases. The factors responsible for marketing sickness, which results in SSI maladies, are grouped on the basis of key elements of marketing. The factors are ranked with the help of Garretts Ranking principles.

The reveals that the following factors have vibrant and more influence on marketing sickness of SSIs.

Problem of delay in payment	Problem of price variation
Lack of finance resources	Acute competition
Lack of entrepreneurial background	Poor quality of the product
Lack of support from the government	Giving long credit period

These factors, ranked first in each group, are the most influential factors responsible for the severe marketing sickness.

7. Sickness of Small Scale Industries in TELANGANA

Sickness [ix]among small-scale industries (SSIs) is rather high in TELANGANA. Among the registered SSI units, the percentage of closed industries is as high as 38 percent.

Translated into numbers, the closed SSI units are a whopping 38,788 out of the total registered number of 1,02,761. The working SSIs number 63,973, according to statistics available with the State Industries Department.

The sickness seems to be particularly rampant in the districts of Hyderabad (50 percent), Nalgonda (48 percent), Medak (47 percent) and Khammam (46 percent), as per the third census report of SSI units in the State.

In efforts to receive and rehabilitate the closed units, the State Government has appointed five institutes to go into the issues of economic viability and work out a package.

These are the National Institute for Small Industries Extension & Training (NISIET), the Small Industries Services Institute (SISI), the TELANGANA Industrial Technology Consultancy Organisation (APITCO), the AP Productivity Council and the Federation of TELANGANA Small Industries Association AP SSI Centre.

These organizations have undertaken a district-wise study of the closed SSI units closed the economic viability of their revival and rehabilitation and will submit a report by the end of July. Based on their recommendations a strategy would be devised.

The national percentage of closed units is 37.65 percent or 8,68,021 units out of the total 23,05,725 registered units surveyed under the Third All-India Census of Small-Scale Industries by the Development Commissioner, Union Ministry of Small-Scale Industries.

For TELANGANA, which has logged higher than the national percentage of units closed, the gratifying feature is that it does not find itself among the top five.

These States are Tamil Nadu (16.2 per cent), Uttar Pradesh (13.4 per cent), Kerala (8.4 per cent), Madhya Pradesh (7.4 per cent) and Maharastra (7.1 per cent). For TELANGANA, the percentage of closed units is 4.2.

CLOSED SSIs THE TOP 10 DISTRICTS				
District	Registered units	Units working	Units closed	% of closed
Hyderabad	8,010	4,034	3,976	50
Nalgonda	5,293	2,768	2,525	48
Medak	3,190	1,696	1,494	47
Khammam	3,374	1,819	1,556	46
Adilabad	1,170	661	509	44
KAMMAM	4,743	2,680	2,063	43

Under the survey, the AP Industries Department also undertook a count of the registered SSIs for the time.

The exercise covered 1,546 villages and towns and a total of 16, 979 units.

REFERENCES

[i] Dr. Vasanth Desai, Management of Small Scale Industry, Himalaya Publishing House, Tenth Edition: 2003, Page No. 618.

[ii] Agarwal, K,. Abha, “Working of sick Small Scale units in the industrial Estates of Kumaun” year 2002.

[iii] Dr. Vasanth Desai, Management of Small Scale Industry, Himalaya Publishing House, Tenth Edition: 2003, Page No. 619.

[iv] Credit and Fiscal concession to small Scale industries, Facts For You, Vol. 25, October 2004, Page No. 31.

[v] Annual Report of Industrial Development Bank of India, 1986-87.

[vi] Pradip N Khandawalla, The performance determinants of public enterprises: Case studies of four equipment manufacturing Indian public enterprises. A study commissioned by the World Bank, 1981.

[vii] Report of the Working Group on Rehabilitation of Sick SSI Units constituted by RBI of 2001.

[viii] S.Murugan, Dr. M. Edwin Gnanadhas, Dr, N. Thaiavai Pillai, Indian Journal of Marketing, Vol: XXXIV, No.: 5, May 2004.

[ix] M.Somasekhar, State registers high incidence of sickness among SSIs, The Hindu Business line – June 29, 2004.