



A Study of Small Scale Sector in India

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Introduction:

The Small Scale sector is a significant contributor to the Indian economy. Based on official figures from the Ministry of Small Scale, 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, It 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 Small Scale 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 Small Scale 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.

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 (SSSBs) where investment in fixed assets, excluding land and building was less than Rs.1 million. Looking at the size and significance of Small Scale sector in Indian economy, we note that as of 2004, there were a total of 130 lakhs micro and small firms in India. The number of firms in the Small Scale sector comprises a staggering 95% of all industrial units in India. Together they employ



more than 8% of the total Indian labor force of 509 million individuals. This amounts to a significant 41 million people who are currently employed in this sector. The Small Scale sector is a significant contributor to India's exports amounting to 40% of the total share. It also comprises a lion's share (45%) of the total manufacturing output of the country.

By looking at the decomposition between registered and unregistered units. Of the total, a dominant 86% belong to the unregistered sector. When we take a closer look at the reasons for non-registration of units, we find that 54 percent of all units that were surveyed in the All India Census of SSIs in 2002 cited "not aware of such a provision" as a reason. The next most common reason is "not interested" while a smaller proportion yet cited "complicated procedures" as a reason for non-registration. This highlights the primary reason for including measures to simplify registration process in the Small Scale Act of 2006.

Registration is voluntary in the SSI sector. Looking at the disaggregated data for registered and unregistered firms, we find that although registered units comprise only 13 percent of the sector but in terms of investments, their share is 59 percent and they contribute close to 56 percent of the total production in the sector. Compared to the Second Census data, which was collected in 1988, in the Third Census (2002), we find that per unit employment has gone down in registered units from 6.29 to 4.48. The per unit fixed investment has on the other hand gone up multifold from Rs.1.60 lakhs to Rs.6.68 lakhs.

To understand the true complexity behind the sector, we have to look beyond simple classification of units along registered and unregistered categories. Based on their location, the units can be classified as rural (55 percent) or urban (45 percent). There are further classifications based on the main source of power used in the firm such as electricity (47 percent), no power needed (40 percent), oil (5.6 percent), coal (4 percent) etc. Another interesting fact is that about 11 percent of all small scale units are women managed enterprises.

In the sector as a whole, about half of all units are engaged in services (49 percent). The significance of the services segment in the SSI sector has been



steadily increasing over the last two decades. When we look at the decomposition of units across registered and unregistered units, we notice a majority of registered firms are in the manufacturing, assembling and processing space (62 percent). Another point to note is that there is enormous variation across states within India when we look at the Small Scale sector data. When we consider all registered units, we find that six states have 62 percent of all working units. These states are Tamil Nadu, Uttar Pradesh, Kerala, Gujarat, Karnataka and Madhya Pradesh. The maximum number of unregistered units (17 percent) was located in one state, Uttar Pradesh.

The registered units employ more than twice the number of workers as the unregistered. But this could reflect the fact that unregistered units have a greater number of temporary workers who might not show up on the pay rolls. In terms of the size of firms, measured as per unit fixed investments, registered units are nearly 5 times as large as the unregistered ones.

While studying the Small Scale sector in India, it is crucial to also look into the health of firms because a significant number of firms both within the registered as well as the unregistered sector are defined as 'sick'. Sickness is typically identified through a yardstick and the typical yardsticks are a) delay in repayment of loan over one year (RBI definition), b) decline in net worth by 50 percent and c) decline in output in last three years.

All yardsticks combined reveal that about 14 percent of all units in the SSI sector was identified to be either sick or incipient sick, while this was 6.89 percent for all unregistered units and 7.82 for all registered units. Even here, there is widespread variation across states and a maximum number of all sick units (60 percent) of all sick units are located in West Bengal, Kerala, Maharashtra, Karnataka and Andhra Pradesh. Based on units having loan outstanding with institutional sources like banks and financial institutions, sickness is about 20 percent in the registered SSI sector and 17 percent in the case of unregistered SSI sector. In the total SSI sector, this percentage is about 18 percent. Incipient sickness identified in terms of continuous decline in gross output was 11.5 percent in the registered



sector and 7 percent in the unregistered sector. Detailed data was collected on the various reasons for sickness of firms in the Small Scale sector. The most commonly cited reasons were “lack of demand” and “shortage of working capital”.

The Small Scale sector in India has witnessed significant changes in the post liberalization period since 1991. In this section, we will study the data from 1999 until 2012 and highlight some interesting trends and features of this sector. The first feature we note is that this sector has been growing steadily throughout this period. In 2000 there were 67.07 lakhs Small Scale s in the country. Their number climbed to 113.95 lakhs by 2003.

A fact that might not seem obvious from the graph is that although the proportion of unregistered units remained dominant throughout this period (86.3% in 2003-04), the number of registered firms more than doubled in number over this period. The growth rate for the overall industry and the unregistered segment is steady and close to 4 percent. Once again, given the dominance of unregistered firms it is not surprising that the overall industry growth rate is very closely following the growth of unregistered segment. The growth of registered sector, however, has high variance. This ranges from 14 percent growth to negative growth in few years.

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