

# Role of Small Scale Industries in Indian Economy

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## **Role of SSI in Indian Economy**

Small scale industries play an important role for the development of Indian economy in many ways. About 60 to 70 percent of the total innovations in India comes from the SSIs. Many of the big businesses today were all started small and then nurtured into big businesses.

The roles of SSIs in economic development of the country are briefly explained

### **1. Small Scale Industries Provides Employment**

1. SSI uses labour intensive techniques. Hence, it provides employment opportunities to a large number of people. Thus, it reduces the unemployment problem to a great extent.
2. SSI provides employment to artisans, technically qualified persons and professionals. It also provides employment opportunities to people engaged in traditional arts in India.
3. SSI accounts for employment of people in rural sector and unorganized sector.
4. It provides employment to skilled and unskilled people in India.
5. The employment capital ratio is high for the SSI.

### **2. SSI Facilitates Women Growth**

1. It provides employment opportunities to women in India.

2. It promotes entrepreneurial skills among women as special incentives are given to women entrepreneurs.

### **3. SSI Brings Balanced Regional Development**

1. SSI promotes decentralized development of industries as most of the small scale industries are set up in backward and rural areas.

2. It removes regional disparities by industrializing rural and backward areas and brings balanced regional development.

3. It promotes urban and rural growth in India.

4. It helps to reduce the problems of congestion, slums, sanitation and pollution in cities by providing employment and income to people living in rural areas. It plays an important role by initiating the government to build the infrastructural facilities in rural areas.

5. It helps in improving the standard of living of people residing in suburban and rural areas in India.

6. The entrepreneurial talent is tapped in different regions and the income is also distributed instead of being concentrated in the hands of a few individuals or business families.

### **4. SSI Helps in Mobilization of Local Resources**

1. It helps to mobilize and utilize local resources like small savings, entrepreneurial talent, etc., of the entrepreneurs, which might otherwise remain idle and unutilized. Thus it helps in effective utilization of resources.

2. It paves way for promoting traditional family skills and handicrafts. There is a great demand for handicraft goods in foreign countries.

3. It helps to improve the growth of local entrepreneurs and self-employed professionals in small towns and villages in India.

### **5. SSI Paves for Optimisation of Capital**

1. SSI requires less capital per unit of output. It provides quick return on investment due to shorter gestation period. The pay back period is quite short in small scale industries.
2. SSI functions as a stabilizing force by providing high output capital ratio as well as high employment capital ratio.
3. It encourages the people living in rural areas and small towns to mobilize savings and channelize them into industrial activities.

#### **6. SSI Promotes Exports**

1. SSI does not require sophisticated machinery. Hence, it is not necessary to import the machines from abroad. On the other hand, there is a great demand for goods produced by small scale sector. Thus it reduces the pressure on the country's balance of payments.
2. SSI earns valuable foreign exchange through exports from India.

#### **7. SSI Complements Large Scale Industries**

1. SSI plays a complementary role to large scale sector and supports the large scale industries.
2. SSI provides parts, components, accessories to large scale industries and meets the requirements of large scale industries through setting up units near the large scale units.
3. It serves as ancillaries to large Scale units.

#### **8. SSI Meets Consumer Demands**

1. SSI produces wide range of products required by consumers in India.
2. SSI meets the demand of the consumers without creating a shortage for goods. Hence, it serves as an anti-inflationary force by providing goods of daily use.

#### **9. SSI Ensures Social Advantage**

1. SSI helps in the development of the society by reducing concentration of income and wealth in few hands.
2. SSI provides employment to people and pave for independent living.

3. SSI helps the people living in rural and backward sector to participate in the process of development.

4. It encourages democracy and self-governance.

### **10. Develops Entrepreneurship**

1. It helps to develop a class of entrepreneurs in the society. It helps the job seekers to turn out as job givers.

2. It promotes self-employment and spirit of self-reliance in the society.

3. Development of small scale industries helps to increase the per capita income of India in various ways.

4. It facilitates development of backward areas and weaker sections of the society.

5. Small Scale Industries are adept in distributing national income in more efficient and equitable manner among the various participants of the society.

### **What are the problems faced by Small Scale Industries in India?**

Small Scale Industries do not enjoy much of the advantages enjoyed by large scale enterprises because of their nature and size. Though they have made significant contribution to economic development, they have not realized their full potential. They face many problems in their functioning and many Small-Scale Industries are sick.

The government had reserved certain items for exclusive production by Small Scale Industries. Large scale enterprises were not allowed to produce the items which were reserved for the SSI sector. With the opening up of the economy and following the principles of liberalization and globalization, many items have been successively De-reserved. Therefore Small Scale Industries have to now counter the twin forces of competition from Indian large scale enterprises as well as foreign competitors.

### **Problems faced by Small Scale Industries**

The following are the problems faced by Small Scale Industries:

#### **1. Poor capacity utilization**

In many of the Small Scale Industries, the capacity utilization is not even 50% of the installed capacity. Nearly half of the machinery remains idle. Capital is unnecessarily locked up and idle machinery also occupies space and needs to be serviced resulting in increased costs.

## **2. Incompetent management**

Many Small Scale Industries are run in an incompetent manner by poorly qualified entrepreneurs without much skill or experience. Very little thought has gone into matters such as demand, production level and techniques, financial availability, plant location, future prospects etc. According to one official study, the major reason for SSI sickness is deficiency in project Management i.e., inexperience of promoters in the basic processes of production, cash flow etc

## **3. Inadequate Finance**

Many Small Scale Industries face the problem of scarcity of funds. They are not able to access the domestic capital market to raise resources. They are also not able to tap foreign markets by issuing ADR's (American Depository Receipts) GDR's (Global Depository Receipts) etc because of their small capital base. Banks and financial institutions require various procedures and formalities to be completed. Even after a long delay, the funds allocated are inadequate.

Bank credit to the small scale sector as a percentage of total credit has been declining. It fell from 16% in 1999 to 12.5% in 2002. Small Scale Industries are not able to get funds immediately for their needs. They have to depend on private money lenders who charge high interest. Finance, as a whole, both long and short term, accounts for as large as 43% of the sector's sickness.

## **4. Raw material shortages**

Raw materials are not available at the required quantity and quality. Since demand for raw materials is more than the supply, the prices of raw materials are quite high which pushes up the cost. Scarcity of raw materials results in idle capacity, low production, inability to meet demand and loss of customers.

## **5. Lack of marketing support**

Small Scale Industries lack market knowledge with regard to competitors, consumer preferences, market trends. Since their production volume is small and cannot meet demand for large quantities their market is very restricted. Now with the process of liberalization and globalization they are facing

competition from local industries as well as foreign competitors who sell better quality products at lower prices. For e.g. heavily subsidized but better quality imports from China has made most of the Indian SSI units producing toys, electronic goods, machine tools, chemicals, locks and paper etc., unviable.

## **6. Problem of working capital**

Many Small Scale Industries face the problem of inadequate working capital. Due to lack of market knowledge their production exceeds demand, and capital gets locked in unsold stock. They do not have enough funds to meet operational expenses and run the business.

## **7. Problems in Export**

They lack knowledge about the export procedures, demand patterns, product preferences, international currency rates and foreign buyer behavior. Small Scale Industries are not able to penetrate foreign markets because of their poor quality and lack of cost competitiveness. In countries like Taiwan, Japan etc. products produced by Small Scale Industries are exported to many foreign countries. But in India not much thought and focus has gone into improving the export competitiveness of Small Scale Industries.

## **8. Lack of technology up-gradation**

Many Small Scale Industries still use primitive, outdated technology leading to poor quality and low productivity. They do not have adequate funds, skills or resources to engage in research and development to develop new technologies. Acquiring technology from other firms is costly. Therefore Small Scale Industries are left with no choice but to continue with their old techniques.

## **9. Multiplicity of labor laws**

One of the merits of Small Scale Industries are that they are labor intensive and can provide employment to a large number of people. But the multiplicity of labor laws, need to maintain several records (PF, ESI, Muster Rolls etc), fines and penalties for minor violations etc place Small Scale Industries at a great disadvantage.

## **10. Inability to meet environmental standards**

The government lays down strict environmental standards and Courts have ordered closure of polluting industries. Small Scale Industries which are already

facing shortage of funds to carry out their business are not able to spend huge sums on erecting chimneys, setting up effluent treatment plants etc.

### **11. Delayed payments**

Small Scale Industries buy raw materials on cash but due to the intense competition have to sell their products on credit. Buying on cash and selling on credit itself places a great strain on finances. The greater problem is payments are delayed, sometimes even by 6 months to one year. It is not only the private sector but even government departments are equally guilty. Delayed payments severely impact the survival of many Small Scale Industries.

### **12. Poor industrial relations**

Many Small Scale Industries are not able to match the pay and benefits offered by large enterprises, because their revenues and profitability are low and also uncertain. This leads to labor problems. Employees fight for higher wages and benefits which the SSI is not able to provide. This may lead to strikes, resulting in damage to property in case of violence by employees, production losses etc.

### **13. Strain on government finances**

Marketing of products manufactured by Small Scale Industries is a problem area. The government has to provide high subsidies to promote sales of products produced by Khadi and Village Industries. This places a great strain on government finances.

### **14. Concentration of industrial units**

There is high concentration of small scale industrial units in a few states. Of the estimated 1.37 million registered units as on 2020-21, nearly 35% were located in three states. Uttar Pradesh, Tamil Nadu and Kerala alone account for 35% of Small Scale Industries. Due to concentration, there is high competition among them to procure raw materials and other industrial inputs. This leads to high costs and scarcity of raw materials and other inputs affecting their production and increasing costs.

### **15. Inadequate dispersal**

One of the objectives of the government in promoting Small Scale Industries was to increase industrial development and employment opportunities throughout the country. Since nearly 60% of the Small Scale Industries are concentrated in few states, the objective of balanced regional development and

promotion of backward areas has not been achieved. Further majority of Small Scale Industries are located in urban areas and the aim of industrial development in rural areas has also been defeated.

### **16. Widespread sickness**

Sickness among Small Scale Industries is widespread. Sickness is not detected in the initial stages and large amount of funds are locked in them. Due to this new entrepreneurs are not able to get loans, workers in the sick units lose their jobs and industrial and economic development is affected.

### **17. Lack of awareness**

The government has set up many organizations to support and provide assistance to Small Scale Industries. But, many of the entrepreneurs running Small Scale Industries are not aware of the various support services.

### **18. Government interference**

Small Scale Industries have to maintain a number of records and there are endless government inspections. A lot of time, money and effort is wasted in complying with various inspections and records verification. This prevents Small Scale Industries from fully concentrating on their business activities.

## **Advantages or Merits of Small Scale Industries**

Small Scale Industries have always played an important role in the economic development of the country. The following are the merits of Small Scale Industries:

### **1. Potential for large employment**

Small Scale Industries have potential to create employment opportunities on a massive scale. They are labor intensive in character. They use more labor than other factors of production. They can be set up in short time and can provide employment opportunities to more number of people. This is important for a labor abundant country like India.

### **2. Requirement of less capital**

Small Scale Industries require less capital when compared to large scale industries. India is a capital scarce country and therefore Small Scale Industries



are more suitable in the Indian context. They can be started and run by small entrepreneurs who have limited capital resources

### **3. Contribution to industrial output**

Products manufactured by Small Scale Industries form a significant portion of the industrial output of the country. They produce a number of consumer goods as well as industrial components in large quantities and satisfy the needs of consumers. The consumer goods produced by Small Scale Industries are cheaper and satisfy the requirements of the poorer sections.

### **4. Contribution to exports**

Small Scale Industries contribute nearly 40 per cent to the industrial exports of the country. Products such as hosiery, knitwear, hand loom, gems and jewellery, handicrafts, coir products, textiles, sports goods, finished leather, leather products, woolen garments, processed food, chemicals and allied products and a large number of engineering goods produced by the SSI sector contribute substantially to India's exports. Further products produced by Small Scale Industries are used in the manufacture of products manufactured and exported by large scale industries. Therefore they contribute both directly and indirectly to exports and earn valuable foreign exchange.

### **5. Earning foreign exchange**

Small Scale Industries earn valuable foreign exchange for the country by exporting products to different countries of the world. At the same time, their imports are very little and so there is less foreign exchange outgo. Therefore Small Scale Industries are net foreign exchange earners. For e.g. Small Scale Industries in Tiruppur contribute to a substantial portion of India's textile exports and earn valuable foreign exchange for the country.

### **6. Equitable distribution**

Large scale industries lead to inequalities in income distribution and concentration of economic power. But small scale industries distribute resources and wealth more equitably. It is because income is distributed among more number of workers since it is labor intensive. This results in both economic and social welfare.

### **7. Use of domestic resources**

Small Scale Industries use locally available resources in a productive manner which would have otherwise gone waste. Small amounts of savings which would have remained idle is channelized into setting up of small enterprises. This increases capital formation and investment in the economy.

### **8. Opportunities for entrepreneurship**

Small Scale Industries provide opportunities for entrepreneurs with limited capital. Setting up of an SSI requires less capital and lower investment in technology and machines when compared to large scale enterprises. Therefore small entrepreneurs can start Small Scale Industries easily and succeed. Japan which was devastated by the Second World War became a major economic power because of many small entrepreneurs, who contributed greatly to the nation's development.

### **9. Cost efficiency**

Small scale units can adopt lean production method, which offer better quality and more variety at a lower cost. They can be more cost efficient when compared to large scale units because their expenses are lower.

### **10. Reducing migration**

Migration happens when people living in rural areas are not able to find employment and therefore migrate to urban areas seeking employment. Large scale migration puts tremendous pressure on land, water and other resources in urban areas leading to poor quality of life. Small Scale Industries use the skills and talents of rural craftsmen, artisans etc. They provide gainful employment to those with inherited skills resulting in their economic upliftment. Thus Small Scale Industries help in reducing migration.

### **11. Suitable for non-standardized products**

Large scale enterprises are suitable for manufacturing standardized products on a large scale whereas Small Scale Industries are more suitable for manufacturing non-standardized products.

### **12. Flexibility in operation**

Small scale enterprises are more flexible. They can adapt themselves to changing market requirements very fast and benefit from new opportunities.

### **13. Quick decisions**

Since the enterprise is small and there is not much hierarchy, quick decisions can be taken. Quick decisions are helpful in solving problems in the initial stages and also to exploit market opportunities.

#### **14. Adaptability to change**

Small Scale Industries can understand the changing requirements of the customers and adapt themselves much quickly. They can change their procedures, methods and techniques faster and cater to new requirements of their customers.

#### **15. Small market size**

In case the market size is small, producing products on a large scale would not be feasible. In such cases, Small Scale Industries are more suitable since they produce limited quantities.

#### **16. Customization**

Today customers prefer products tailored to their specific needs. They demand unique products. In such cases where products have to be customized to individual customer needs large scale production would not be suitable. Small Scale Industries are better suited in case products have to be customized.

#### **17. Low social costs**

In the case of large scale enterprises, society has to incur high social costs in terms of air and water pollution and environmental degradation. But in the case of small enterprises, such social costs are less.

#### **18. Opportunity for talent**

Small Scale Industries provide opportunity for talented individuals who do not have huge funds, to start enterprises on a small scale. Dhirubhai Ambani of Reliance, Karsanbhai Patel of Nirma, Brij Mohan Munjal of Hero Honda, Venugopal Dhoot of Videocon, Sunil Mittal of Bharti Enterprises (Airtel), Narayanamurthy and his co-promoters of Infosys, Ramalinga Raju of Satyam are all examples of entrepreneurs who started their business on a small scale, and through intelligence, determination and commitment have transformed their small companies into large world class players.

#### **19. Lesser industrial disputes**

In large scale enterprises workers are more organized and in many large scale enterprises there are strong trade unions. The trade unions fight for the workers rights. If the management fails to accept the demands of the trade unions, the trade unions gherao the management, adopt go slow tactics and strike work. But in small scale enterprises, workers are not well organized and union activity is less. So there is very little possibility of industrial disputes to occur.

## **20. Personal contact with employees**

Businesses engaged in small scale production have less number of employees. It is easy to maintain personal contact with employees. Grievances and problems would be known immediately and solved. Therefore there is very little possibility of any industrial dispute.

## **21. Personal contact with customers**

The number of customers is limited and the small scale entrepreneur would be directly involved in the business. Personal contact can be maintained with customers. Their needs and requirements can be understood and satisfied. This results in satisfied customers leading to stable demand.

## **22. Self interest**

Small business is generally run by the sole proprietor of the business. He earns all and risks all. Self-interest act as a strong motivator. Therefore, he would put in his best efforts to make the business a success.

## **Demerits or Disadvantages of Small-Scale Industries**

Though small scale industries have several advantages they suffer from the following demerits:

1. **Lack economies of scale:** SSI's produce in small quantities. Therefore they **do not enjoy economies of scale** in purchases, production and marketing. Their costs are consequently higher and they are not able to compete with large scale units. They were able to survive when many of the items were reserved for production by SSI's. But after the economic liberalization policy followed by the government, many of the items have been De-reservad. Therefore large scale units can also produce products which were earlier produced only by small scale units. Many of the SSI's have closed down unable to compete with large scale producers and cheap imports from other countries, especially China.

2. **Low wages:** Though SSI's are labor intensive, the **wages paid in SSI's are low** when compared to those paid in large scale industries. In many SSI's because of **lack of safety measures** and proper training to workers, accidents and injuries are common occurrences.

3. **Lack of modernization:** Due to their small scale of operations and limited capital resources, SSI's are not able to invest in modernization. They **do not have access to latest technology** and therefore cannot improve their efficiency of operations.

4. **Inefficiency:** Due to lack of scale economies, low skilled and poorly trained workers and usage of outdated technology, small scale industry suffers from **inefficiency of operations**. Their productivity is low when compared to large scale industries.

5. **Overcrowding:** It is quite easy to set up an SSI. The capital requirement is less and procedural formalities are simple. This leads to **intense competition and overcrowding**. It may lead to cut-throat competition affecting their survival.

6. **Sickness:** Due to the ease of setting up and because of the incentives available, many unemployed youth set up SSI's with very little business knowledge and skills. They find it difficult to survive in the business and close down their operations. Further because of the **problems of procuring finance**, use of **outdated technology** and **lack of marketing expertise** many SSI's incur losses and are forced to close down.

7. **Less innovation capacity:** SSI's have limited financial resources, therefore they are **not able to invest adequately in research and development (R&D)** or acquire technology. As a result their technological up-gradation is less and they continue with outdated processes and techniques. This hinders their competitiveness and capacity to come out with new products, processes etc.

8. **Low competitiveness:** Due to their small scale, lack of modern technology and poorly trained workers, SSI's **lack the competitiveness to compete with large scale industries**. Now, many items which were reserved for production by SSI's have been De-reserved. Therefore SSI's face increasing competition from large scale Indian enterprises as well as foreign competitors.

9. **Low capacity utilization:** In many SSI's, **capacity utilization is low and productive capacity remains idle**. Small firms are unable to utilize their full capacity due to problems related to finance, marketing, technology, skills etc.

10. **Lack of pollution control:** Large scale enterprises which are polluting in nature, are able to set up pollution control equipment such as effluent treatment plants. SSI's are not able to set up such facilities because of lack of finance, technology, skills etc.

11. **Low labor productivity:** The **productivity of labor in small scale industries is low**. The reason is workers employed in SSI's are unskilled, lack proper training and work on outdated technology. Their wages are less and therefore motivation levels of workers is also quite low. Poor labor productivity results in lower output, increasing the cost of production and problems in meeting demand schedules.

### **Measures to Promote Small Scale Industries in India**

Small Scale Industries have contributed a lot for the development of the economy of India. Still SSI face problems due to the nature and size of their business. Some of the measures that can be taken by government and NGOs to boost the performance are as follows:

1. Government should ensure that adequate financial assistance is provided to SSIs through banks and financial institutions. The rate of interest on loans should be low. Financial assistance must be provided to SSI through unsecured loans or after obtaining minimum security.

2. Insurance coverage must be extended to new and existing small scale industries.

3. The gap that exists between consumers and small business must be bridged through effective marketing. Lot of industrial fairs, exhibitions must be organized by the government to encourage the sale of SSI products.
4. The infrastructural facilities must be improved and measures must be taken to enhance the supply of water, electricity to backward and rural areas.
5. Technological support must be provided to SSI to import machinery at lower cost.
6. Many industrial estates must be established by the government.
7. The informal money market should be regulated to avoid exploitation by money lenders on small scale industrialists.
8. Training must be provided to entrepreneurs in technological, managerial, financial and marketing areas.
9. Awareness campaigns must be carried out in full swing to encourage youngsters to become first generation entrepreneurs.
10. The sick industries must be rejuvenated instead of liquidation.
11. The licensing procedure must be simple and at ease.
12. Fair Incentives and subsidies must be given to SSI units and an awareness must be made about the incentives available to new entrepreneurs
13. Export promotion schemes must be devised in such a way that encourages SSI to export their goods.