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# INDIA: THE ROLE OF SMALL-SCALE INDUSTRIES IN AN EMERGING 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. Conclusions drawn from the analysis of the data suggest that the various policy initiatives taken by the Government of India since independence have helped this sector to grow considerably. Some of the policies of the Government of India may, however, not be very helpful in increasing the efficiency of units in this sector as number of non-viable units is increasing steadily.

## 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 for consumer goods. These units also help in solving the problem of regional disparities in economic growth (Gyan Prakash, 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 effect 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 2 of this paper, the legal framework relating to small-scale industries in India is explored. In section 3, the macroeconomic contribution of small-scale industries to India's economy is evaluated. In section 4, the availability of credit to SSI units from public sector banks are discussed. In section 5, issues relating to sickness of the SSI units are examined. The policy issues and future prospects are analysed in section 6. Finally, an analysis of the performance of SSI sector is undertaken in Section 7 and conclusions are drawn from this analysis.

## **LEGAL FRAMEWORK**

The term small-scale industry used in India is a kind of misnomer. This term is used to indicate small sized industrial units and not small sized industries. The legal framework is provided by Industries Development and Regulation Act, 1951 (IDR ACT) Section 11B of this Act specifies the general requirement that are to be complied by the small-scale industrial units. The sub-section 11B(1) of I.D.R.Act defines small-scale industrial undertaking "*as an industrial undertaking which may be held on ownership terms, lease or hire purchase basis and the original investment in plant and machinery in that undertaking does not exceed the specified limit in force at the time.*" Table 1 indicates the historic evolution of this definition of small-scale industry in India. In addition to small-scale industrial undertakings, the IDR Act 1951 also refers another category of small-scale industrial undertaking called Ancillary Industrial Undertakings. This ancillary industrial undertaking is a part of small-scale sector. Over the years, some other sub-sectors have been included within overall small-scale sector.

Tiny Enterprises  
Export oriented Units

*Small-scale Service and Business Enterprises  
Women Enterprises.*

The SSI sector in India covers a wide spectrum of industrial units categorised under small, tiny and cottage segments. The term Small-scale Industry evokes different meaning to different agencies of the government in India. For example, the Planning Commission of the Government of India regards the Village and Small Industries (VSI) sector as a part of SSI sector. The Central Excise Department distinguishes SSIs on the basis of the turnover (Up to a maximum of Rs. 30 million). The legal nomenclature developed by the government is very complicated. This is evident from the many classes and sub-classes adopted in defining the small-scale industry. Further the rules relating to eligibility of industrial units as SSIs are also not very easy to interpret. The calculation of the value of plant of machinery depends on a number of things in addition to the price paid to the vendor. For example, cost of installation and inland transport charges paid in India are not included in value of plant and machinery whereas import duty and shipping charges on imported machinery are included. It is therefore very difficult to make a meaningful comparison or statistical analysis of SSI units in India based on the evolution of legal definition adopted by the Government of India and given in table 1. (Ministry of SSI, Govt. of India, Annual Report, pg.5)

From Table 1, it can be seen that the definition of the eligibility for small-scale industry has undergone many changes in India since 1950. Initially the capital assets were included as the basis of categorising a unit as a small scale unit. Since 1966 only the original value of plant and machinery is considered for the purpose of SSI classification. From 1966 to 1997, the limits on the value of plant and machinery, has consistently increased. But in 1998 this limit was considerably lowered to Rs.10 millions from Rs.30 millions. This was a period when the Government of India started a policy of economic rationalisation for small-scale industries, which is still continuing under pressure from World Trade Organisation. (Raju, 2001). Although the limit on the value of plant and machinery was lowered in 1998 the number of SSI units operating in India still increased in 1998-99. The growth rate in the number of SSI units however, declined in 1998-99 to 3.55% as compared to 5.5% in 1997-98 suggesting that the decrease in the growth rate of the number of SSI units could be due to the change in the eligibility criterion.

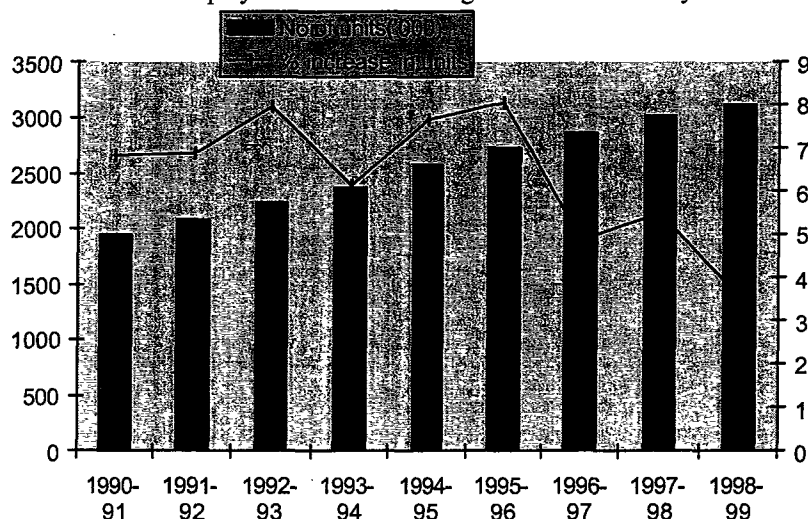
**Table 1: Evolution of the definition of SSI in India**

Year	Capital
1950	Capital assets not exceeding Rs 500,000
1958	Capital investment of less than Rs. 500, 000
1959	In capital investment, the value of machinery to be taken at the original price paid irrespective of it being new or old
1960	Gross value of fixed assets up to Rs. 500,000
<b>Original Value of Plant and Machinery Only</b>	
1966	Up to Rs. 750,000
1975	Up to Rs. 1.0 million
1980	Up to Rs. 2.0 million
1985	Up to Rs. 3.5 million
1991	Up to Rs. 6.0 million
1997	Up to Rs. 30.0 million
1998	Up to Rs. 10.0 million.

*Data source. Ministry of Small-scale Industries & Agro and Rural Industries, Government of India, Annual Report 1999 - 2000, Page 4.*

### CONTRIBUTION OF SSI SECTOR TO INDIA'S ECONOMY

The SSI sector in India plays a vital role in the growth of the country. It contributes



**Figure 1. Graph showing the number of SSI units in India and % increase in the number of units from 1990-91 to 1998-99.**

*Data source: Ministry of Small-scale Industry, Government of India, Annual Report, 1999-2000.*

40% of the gross manufacture to the Indian economy. It has been estimated that 100 thousand rupees of investment in the small-scale sector produces 462 thousands worth of goods and services with an approximate value addition of ten percentage points (SIDO, 2000).

The SSI sector has grown rapidly over the years. The growth rate is very impressive. The number of small-scale units has increased from an estimated 874 thousand units in 1980-81 to 3.121 million units in the year 1998-99. The employment in SSI sector has increased from 12.53 million persons in 1990-91 to 17.16 million persons in 1998-99. The rate of growth in the number of SSI units in India is given in Figure 1.

From the year 1990-91 this sector has exhibited a lower growth trend. This has to be viewed in terms of general recession in the economy. The transition period of the process of economic reforms was also affected for some period by adverse factors such as foreign exchange constraints, credit squeeze, demand recession and high interest rates. During 1994-95 and 1995-96, the trend was reversed. After 1997-98 the growth rate was reduced possibly due to the effect of Asian Financial Crisis and also due to the change in the legal definition of SSI units, which resulted in the decrease in the original cost of plant and machinery, which could be covered in SSI sector.

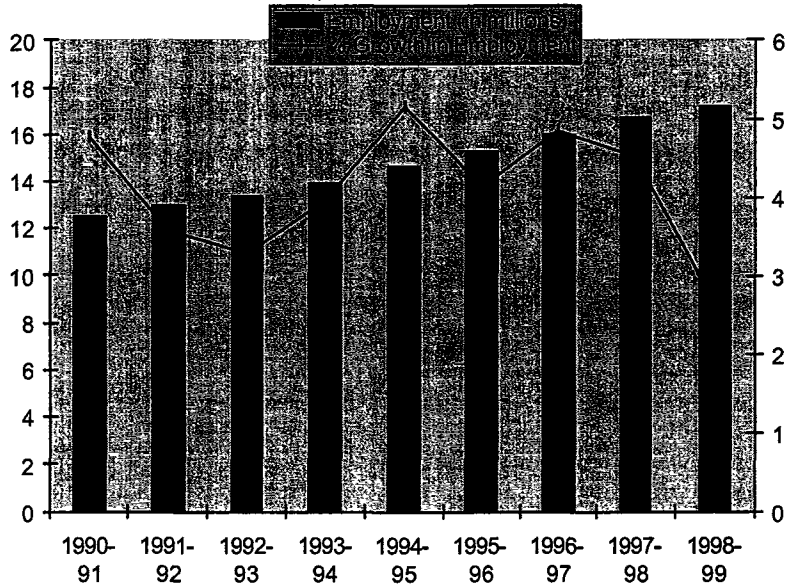
The rate of employment growth in SSI sector in India between 1990 and 1999 is about 3-5% per year as is evident from Table 2 and Figure. 2. The SSI sector is particularly suited for employment growth in a country like India because SSIs are more labour intensive than larger industries, which are capital intensive. The labour intensity of SSIs enables them to provide employment to millions. Further SSIs also help in solving the problem of regional disparities in employment in India by maximising employment opportunities in rural and semi-urban areas. One of the disadvantages of

**Table 2: Growth in number of units and employment in SSI sector in India**

Year	Number of Units In thousands	% Growth in no. of units	Employment (No. of persons) in millions	% Growth in employment
1990-91	1948	6.86	12.53	4.77
1991-92	2082	6.88	12.98	3.59
1992-93	2246	7.98	13.406	3.28
1993-94	2381	6.14	13.938	3.97
1994-95	2571	7.66	14.656	5.15
1995-96	2724	8.05	15.261	4.13
1996-97	2857	4.88	16.00	4.84
1997-98	3014	5.5	16.72	4.5
1998-99	3121	3.55	17.158	2.62

*Data source. Ministry of Small-scale Industries & Agro and Rural Industries, Government of India, Annual Report 1999 - 2000, Page 4.*

using labour intensive technology is that such a technology may render production costly and eventually uneconomical. However if this happens then there should be a decline in the growth rate of new SSI units in India, which has not happened as is evident from Figure 1.

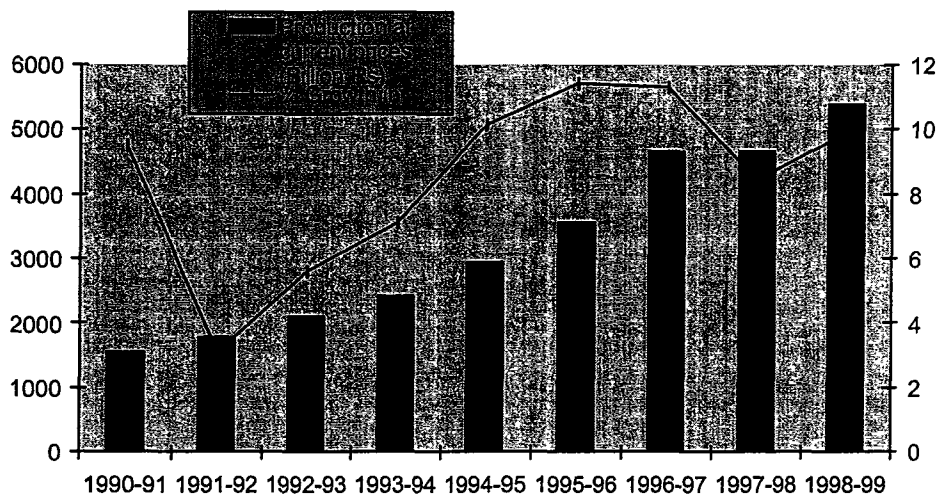


**Figure 2. Graph showing the employment in SSI sector in India (in million persons) and % growth in employment from year 1990-91 to 1998-99.**

*Data source: Ministry of Small-scale Industry, Government of India, Annual Report, 1999-2000.*

The choice still remains between maximising efficiency and increasing employment.





**Figure 3. Graph showing the Production by SSI sector in India (at current prices) and % growth in production from 1990-91 to 1998-99.**

*Data source: Ministry of Small-scale Industry, Government of India, Annual Report, 1999-2000.*

SSIs in India help in solving employment problem to some extent although efficiency may be compromised.

**Table 3: Growth in production and exports by SSI sector in India**

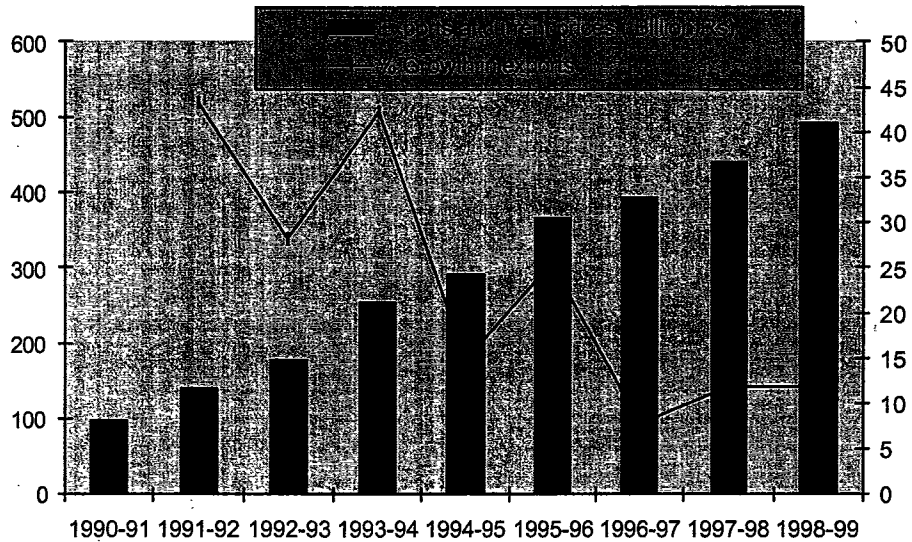
Year	Production		Exports	
	At current prices (Billions of Rs)	%Growth at constant prices 1990-91	at current prices (Billions of Rs)	Growth %
1990-91	1553.40	9.46	96.64	
1991-92	1786.99	3.10	138.83	43.3
1992-93	2093.00	5.60	177.85	28.1
1993-94	2416.48	7.10	253.07	42.3
1994-95	2939.90	10.1	290.68	14.86
1995-96	3562.13	11.40	364.70	25.46
1996-97	4126.36	11.3	392.49	7.62
1997-98	4651.71	8.43	439.40	11.95
1998-99	5383.57	9.91	491.81	11.92

*Data source. Ministry of Small-scale Industries & Agro and Rural Industries, Government of India, Annual Report 1999 - 2000, Page 4.*

SSI sector plays a very important role in the production in India. The production figures from 1990-91 to 1998-99 are given in Table 3. The production in the SSI

sector has continuously increased in India from 1990-91 to 1998-99. However, the rate of growth in production has declined in 1997-98 but increased again in 1998-99. The decrease in growth rate in production could be attributed to the change in the legal definition of SSI units because a number of SSI units ceased to be small units with the decrease in the original cost of plant and machinery.

In addition to production, the 45%-50% of the Indian exports are contributed by SSI sector. The export performance of SSI sector in India is given in Figure 4.



**Figure 4. Graph showing the exports by SSI sector in India (at current prices) and percentage growth in exports at constant prices (1990-91).**

*Data source: Ministry of Small-scale Industry, Government of India, Annual Report, 1999-2000.*

Direct export from SSI sector account for nearly 35% of the total exports. The number of small-scale units that undertake direct exports would be about 5000. Small-scale industrial units also contribute to nearly 15% of exports indirectly. This 15% of indirect export takes place through merchant houses, trading houses and export houses. These may also be in the form of export orders from large units or the production of parts and components for use in finished exportable goods. The product groups where SSI sector dominates in exports are sport goods, readymade garments, woollen garments and knitwear, gems and jewellery, plastic products, processed food and leather products.

The growth in SSI sector can be attributed to a series of industry policy resolutions and statements formulated by the Union Government in India, which aimed to promote the industrial growth and encouraged state intervention and assistance. The 1956 Industrial Policy Resolution recognised the role that SSI sector could play in providing employment opportunities, mobilising local skills and resources and integrating SSI sector with larger units. The Industrial Policy Statement of 1977, stressed on the dispersal of cottage and small industries into rural areas and small towns. The concept of District Industries Centre was also for the purpose of providing services to SSI under one roof. In 1980 emphasis was put on the ancillarisation and

creation of nucleus plants whereas Industrial policy in 1990 focussed on enhancing the contribution of SSI sector in exports, employment generation and dispersal of industries into rural areas. The Industrial Policy in 1991 provided a basis for Integrated Infrastructure Development for SSIs with the participation of State Government, Financial Institutions Non-Government Organisations and Industry/Trade Associations. The measures taken by the government include reservation of products for exclusive manufacture by SSIs. 812 items are currently reserved in this category. (SIDO, 2000)

## CREDIT AVAILABILITY

Table 4 shows the position of credit flow to SSI sector in India. Most of the credit to SSI sector in India is provided by public sector banks, which are expected to follow the government policy in the flow of credit. The SSI sector is covered as a priority sector for lending purpose by the public sector banks according to the policy laid down by the Reserve bank of India. However this policy does not apply to private sector and foreign banks in India.

**Table 4**

### Credit to SSI sector from Public Sector Banks in India

(Amount in Rs. Billions)

Net Bank Credit	At the end of March				
	1995	1996	1997	1998	1999
Net Bank Credit	1690.38	1843.81	1896.84	2182.19	2462.03
Credit to SSI	258.43	294.85	315.42	381.09	426.74
No. of SSI accounts (in thousands)	3225	3377	N.A.	2964	N.A.
SSI credit as % of Net Bank Credit	15.29	15.99	16.6	17.5	17.33

Data source: Small Industries Development Organisation: Small-scale Industries in India, <http://www.laghu-udvog.com/sssindia/spfpr01x.htm>.

The percentage of net bank credit to SSI units from public sector banks has increased from 15.29% in 1995 to 17.33% in 1999 against a target of 16% set by Reserve Bank of India for public sector banks. Although the private sector banks and foreign banks are exempt from these regulations, the outstanding credit deployment to the SSI sector from private sector banks was at Rs.64.51 Billion at the end of March 1999 forming a share of 18.9% of their net credit. Outstanding advances to SSI sector from foreign banks aggregated Rs.24.50 Billion at the end of March 1999, accounting for 11% of their net bank credit.

According to Raju (2001), the lack of access of timely and adequate credit is a big hurdle for the development of SSI sector in India. The Adid Hussain Committee constituted by the Reserve bank of India in 1997 examined the problem of credit to SSI sector and recommended the restructuring of financial support to SSI sector because the overall credit availability to SSI sector during 1991-96 was only 13% of the value of production. It is very clear that legislative measures and government policies in regard to financing of SSI units have not been able to address the issue of credit availability to this vital sector of India economy adequately. The involvement of private sector and foreign banks in India in this regard has been very limited. The private sector banks do not have a vast network of branches in India as do the public sector banks. Foreign banks are mostly confined to big cities of India reducing their availability as a creditor to vast number of SSI units, which are located in small towns.

Table 5 gives the status of credit flow to tiny sector, within SSI sector since 1995. As per RBI guidelines, 40% of priority sector lending to SSI has to go to tiny units with investment in plant and machinery below Rs. 500,000 and another 20% to tiny units with investment in plant and machinery between Rs. 500,000 and Rs 2.0 million.

**Table 5 Credit to Tiny Sector as a part of SSI sector in India**

Net Bank Credit (Amount in Rs. Billions)	At the end of March			
	1995	1996	1997	1998
Net Credit	77.34	81.83	95.15	102.73
Tiny Credit as a Percentage of credit to SSI	29.93	27.76	30.2	27.0

*Data source: Small Industries Development Organisation: Small-scale Industries in India, <http://www.laghu-udvog.com/sssindia/spfpr01x.htm>.*

Thus against a target of 60% of SSI credit to tiny units, actual flow is at 27%. RBI has taken a number of steps in recent years to improve the credit delivery mechanism to SSI units such as encouraging public sector banks to open more specialised SSI branches at centres where there is a potential for financing SSI borrowers.

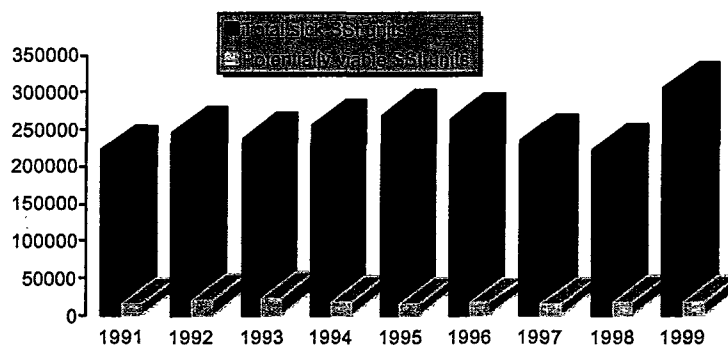
As on March 1998, 370 specialised branches were already working in the country. Other measures include extending single window scheme to meet all financial requirements of term loan and working capital, delegation of enhanced power to branch managers of SSI branches and according the benefit of less spread over prime lending rates to SSI units with a good track record. In spite of all these measures the problems remains.

The directed credit policy of the Government of India has helped in raising the investment in the small-scale industries in India considerably as evidenced by the work of Eastwood et. al (1999; p.58), who are of the opinion that "the view that the efforts minimising official of public sector banks are unlikely to lend to small firms unless forced to do so should not be discounted, making the directed credit somewhat stronger in the case of such banks." Eastwood et. al (1999; p.57) conclude that "directed credit policy in India was well conceived and successful in the case of small

modern sector firms; the financial constraints that the policy was designed to relax does appear to have existed and the extra bank credit channelled to small firms does seem to have raised their investment appreciably".

## SICKNESS IN THE SMALL-SCALE SECTOR

Sickness in the small-scale sector is a matter of great concern in India. Sickness or financial distress results in locking of resources, wastage of capital assets and loss of production in addition to affecting the circulation of bank credit. A number of causes have been attributed to sickness in SSI units in India. Some of these are: faulty planning, management inefficiencies, inefficient financial control, obsolete technology and machinery, diversion of resources, shortage of raw material and other input, power cuts, inadequacy of working capital, delay in the availability of credit.



**Figure 6. Graph showing the total number of sick SSI units and number of potentially viable SSI units in India.**

(Data source: Reserve Bank of India, Annual Report, 1999-2000 .[www.rbi.gov.in](http://www.rbi.gov.in))

The magnitude of sickness can be estimated from the RBI data from 1991 to 1999, given in Figure 6 and Table 6. On the average 10% of SSI units in India face financial distress and only about 67% of distressed units ultimately come out of financial distress and become viable again.

The Reserve Bank of India has issued a number of guidelines to public sector banks for rehabilitation of sick SSI units. The measures suggested by Reserve Bank include detection of sickness at an early stage and grant of relief and concessions such as:

- Interest on working capital at 1.5% below the prevailing fixed/PLR,
- Interest free Funded Interest Term Loan
- Working Capital Term Loan at 1.5% below the prevailing fixed/PLR
- Concession up to 2% below the document rate for Term Loan
- Contingency Loan Assistance at concessional rate for working capital

The Kapur Committee set up by RBI (RBI Annual report 1999-2000) to review the working of the delivery system of credit to SSI units recommended the following measures to deal with sickness

- Changing the definition of classifying the SSI unit as sick unit by reducing the non-performing period of the SSI unit from 21/2 years to one year.

- Converting State Level Inter Institutional Committees into Statutory bodies to enable them to play an effective role in the rehabilitation of sick SSI units.
- Setting up branches of SLIICs in districts having large concentration of SSI units
- Providing relaxation in income recognition and asset classification amounts to encourage banks to take up rehabilitation of potentially viable sick units.

It is too early to estimate the impact of these measures on the sickness in SSI units.

**Table 6: Sickness in SSI sector in India**

As at the end of	Total Sick units		Potentially Viable	
	No.	Amount Outstanding (Rs. Millions)	No.	Amount Outstanding (Rs. Millions)
1991	221,472	27290	16,140	6931.20
1992	245,575	31006.7	19,210	7289.0
1993	238,176	34429.7	21,649	7987.90
1994	256,452	36803.7	16,580	6859.30
1995	268,815	36471.60	15,539	5979.30
1996	262,376	37219.40	16,424	6358.20
1997	235,032	36092.0	16,220	4793.10
1998	221,536	38566.40	18,686	4559.60
1999	306,221	43134.80	18,692	3768.60

*Data source: Reserve Bank of India, Annual Report, 1999-2000 .www.rbi.gov.in*

## **POLICY INITIATIVES**

The importance that the government attaches to SSI sector is reflected in the fact that a new ministry to deal exclusively with small and tiny industries was constituted in 1999. The policy initiatives taken by the Government in India and given in the annual report of Ministry of Small Scale Industries, 1999-2000 in regard to SSI sector can be divided into the following categories.

Financial Concessions

Reservations

Infrastructure Support

Training

Technological Support

Marketing and Export Promotion

Each of these policy initiatives is discussed in detail below.

*a. Financial Concessions.*

From time to time the SSI units have been given a number of financial concessions. Some of the concessions currently available are:

Excise exemptions for branded goods to units located in rural areas. General Excise exemption to industries such as those engaged in cotton yarn and glazed tiles, packaged tea.

Increase in MODVAT Credits to manufacturing units

The other fiscal incentives are by way of concession in credit to SSI units from banks.

Important changes in recent budget include:

Enhancement in the limit of composite loan from Rs. 200,000 to Rs. 500,000.

Delegation of more powers to branch managers to grant ad-hoc facilities to the extent of 20% of limit sanctioned.

Special training programs for branch managers.

Opening of more SSI branches.

Credit insurance scheme.

*b. Reservation*

The reservation of items of exclusive manufacture in SSI sector is statutorily provided for in Industries (Regulation and Development) Act. The reservation policy aims to ensure that the bulk of increased production of consumer goods is in the small-scale sector. The reservation policy also helps in expanding employment opportunities through setting up of more SSI units. 812 items are currently reserved for exclusive manufacture in SSI sector. Non-SSI units can undertake manufacture of reserved items only if they undertake 50% export obligations. There is no regulation or restrictions on marketing of reserved items by large units.

*c. Infrastructure Support*

The government has launched a program of infrastructure development in regional and rural areas. Infrastructure facilities like power, water, communications are funded by the government and SIDBI with the government providing equity and SIDBI providing the loans.

*d. Training*

The Small Industries Development Organisation, through its network of Small Industries Service Institutes is conducting training programs such as Entrepreneurship Development Programs for various target groups for generating employment and upgrading skills in industries such as hosiery, food products, leather products, herbal cosmetics etc. These trainees are given equity assistance and loans for setting SSI units.

*e. Technology Support*

SIDBI had set up a Technology Development and Modernisation Fund for direct assistance of Small-scale Industries to encourage existing industrial units in the sector, to modernise their production facilities and adopt improved and updated technology to strengthen their export capabilities. Assistance is available for meeting capital expenditures, acquisition of technical know how, upgrading of process technology

and total quality management in SSI units. The other forms of technology support include:

Setting up tool rooms and Product cum Process Development Centres

Providing assistance to industry associations/voluntary agencies to set up testing centres.

Industry Specific Institutes for training such as Central Leather Institute.

*f. Export promotion*

Export promotion from the small-scale sector has been accorded a high priority in the India's export promotion strategy because export from this sector accounts for about 40% of total exports. Export strategy for SSI sector includes simplification of export procedures, providing export incentives, trainings and awards etc.

*g. Credit Guarantee Scheme*

The objective of the Credit Guarantee Scheme is to help the SSI units to access credit without the need for a collateral security from eligible financial institutions. The loan limit under the scheme is Rs.2.5 million. The Government of India and SIDBI, the apex development bank have set up a corpus fund of Rs.25 Billion. The fund, which is known as Credit Guarantee Fund Trust for Small Industries (CGTSI) helps in the availability of collateral free credit to the SSI sector. The Member Lending Institutions sanction credit to the eligible borrowers based on the viability of the projects and seek guarantee cover from CGTSI against the payment of one time guarantee fee 2.5% of the sanctioned credit facility and thereafter, annual service fee of 1% on the outstanding credit. CGTSI guarantees up to 75% of the credit subject to loan cap of Rs.2.5 million and guarantee cap of Rs.1.875 million per borrower. The current trend in percentage of default is around 20% (Venkatsubramanyam, 2001). The success of the guarantee scheme will get reflected only when Member Lending Institutions treat the guarantee scheme as an incentive to support the SSI units.

## **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.

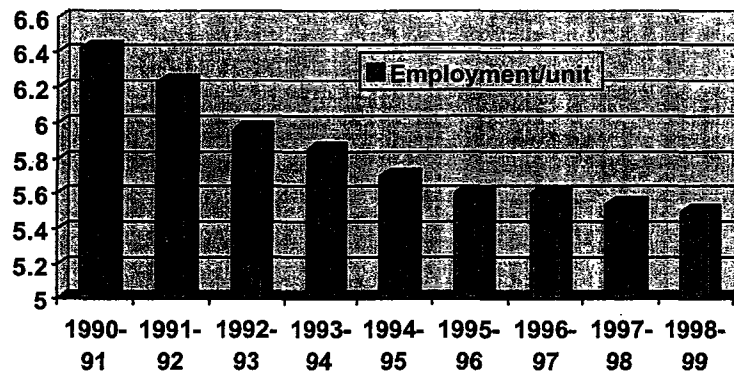
The first criterion discussed by Hallberg(2000) is the share of firms and employment. From the data given in Tables 1,2,3 it is observed that the SSI sector in India has shown considerable growth from 1990-91 in terms of number of units, employment numbers, production and exports. Nearly 40% of India's 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 good items 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.

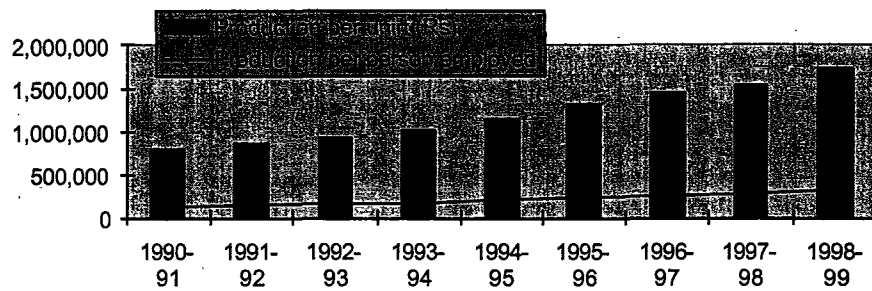
Hallberg (2000) further suggests that "small firms have higher job creation and destruction rates than large enterprises and may offer lesser job security than large firms." In India the destruction rate of SSI firms is close to 9-10% and revival rate of SSI units is very small (only 6-7% of the sick 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. Figure 7 shows the employment per unit in SSI sector in India from 1990-91 to 1998-99.



**Figure 7. Graph showing the employment per unit in SSI sector in India from 1990 -91 to 1998-99.**

Figure 8 shows the production per unit and production per person employed in SSI sector in India from 1990-91 to 1998-99. From Figure 7 and Figure 8, it is observed that the employment per unit in India has declined progressively from 1990-91 to 1998-99 whereas the production per unit and production per person employed has increased during the same period (see also Table 7). This suggests that the SSI sector in India is progressively increasing their efficiency in regard to production and employment.



**Figure 8. Graph showing the production per unit and production per person employed in SSI sector from 1990-91 to 1998-99.**

This increase in relative efficiency has resulted from a very low fixed investment per unit of Rs.208,056 and fixed investment per person of Rs.37,844 (smeindia.com, 2001). These ratios are important for SSI sector in a country like India because India has an intense capital shortage and SSI units in India face a credit shortage as discussed in Section 4.

**Table 7: Efficiency parameters of SSI sector in India**

Year	No. of persons employed per unit	Production (in Rs.)	
		per unit	per person employed
1990-91	6.43	797,433	123,974
1991-92	6.23	858,305	137,672
1992-93	5.96	931,878	156,124
1993-94	5.85	1,014,901	173,373
1994-95	5.70	1,143,485	200,593
1995-96	5.60	1,307,683	233,413
1996-97	5.60	1,444,298	257,897
1997-98	5.54	1,543,367	278,212
1998-99	5.50	1,724,950	313,764

Another important issue in regard to SSI sector is the issue of social, political and equity justification for the promotion of this sector in India. According to Hallberg (2000), "the desire of the governments in promoting SMEs is often based on social and political considerations rather than on economic grounds." In the case of India, the support given to the SSI sector by the government does not seem to be entirely on the social and political considerations because the SSI sector serves a very useful economic purpose in terms of employment, production and exports as is evident from the data given above although the SSI sector also helps in the regional development. The social, political and equity justification of SSI sector in India should also be taken into consideration. The political justification of support to SSI sector is evident from the fact that the legal definition of eligibility of SSI units, have changed off and on, which is based on political considerations (Raju, 1991). The various policy initiatives in regard to financial concessions and lending, reservations of items exclusively for

manufacture in SSI sector, infrastructure and technological support given by the Government of India points to an equity and social justification. However, it should be understood that India is a very diverse country with a huge population and many social, cultural and political problems, which can have a considerable impact on the economy as well. The consequences of not providing support to SSI sector can be disastrous for India. Therefore, Hallberg's (2000) argument that the government support to SMEs is because "they are there" could have some validity for SSI sector in India.

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