

# Status and capacity utilization in small scale industries



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## **ABSTRACT**

Over the past year, the global economic crisis has exerted considerable influence on many business organizations of any size. Large industrial establishments have attempted to manage this crisis in their own ways. Amid all this, SME's are increasingly being brought into focus on account of their huge growth potential. The present study aims at examining the status of small industries, industrial policy and capacity utilization of small industries and the reasons for not utilizing it to the fullest extent. Capacity utilization has been examined taking into account the location of the unit, industry group to which it belonged, year of establishment, form of organization, investment in plant and machinery, the entrepreneur's background and various reasons specified by the entrepreneurs. This study is empirical in nature and it is based on the data collected with the help of questionnaire. Efforts are also being made to offer suggestions.

## **Introduction**

Small and medium enterprises have an important role to play in the present context due to its capacity for employment generation, technological innovation, raising exports and developing entrepreneurial skills. They reduce regional imbalances. They have been accorded a strategic position in the successive five year plans towards fulfilment of our socio-economic objectives and helped to achieve our dictum of growth with equity. Since the early 1990s', Indian SMEs have been exposed to intense competition due to the accelerated process of globalization. But at the same time, globalization has brought new opportunities and challenges to Indian SMEs.

India used to support small and medium industrial sector since independence compared to many developing countries. Series of institutions have been set up by the Central Government, State Governments, and provided financial assistance, technical consultancy, information, technical input, training, legal advice, and marketing support and helped in the healthy development and progress of small and medium industries. But a pertinent question that has often been emerged here, whether their capacity has been utilized to the fullest extent or not. Through this paper an effort is made to study the capacity utilization of small scale and medium industries.

## **Meaning and Definition**

In the Indian context, we have not so far succeeded in giving a definition to small and medium industries. What is neither small nor large industries is being loosely defined as medium industries. Here, the term enterprise encompasses business, services and industries. The Micro, Small and Medium Enterprises Bill, 2006, defined the segment on the basis of investments in plant and machinery. Small enterprises are those with an investment of not more than Rs 50 mn in plant and machinery, and medium enterprises with an investment of over Rs 50 mn but less than Rs 100 mn in plant and machinery. This definition has finally put the segment within a legal framework. Under the Act, enterprises have been categorized broadly into those engaged in (i) manufacturing, and (ii) providing/rendering of services. Both the categories have been farther classified into micro, small and medium enterprises, based on gross investment in plant and machinery for manufacturing enterprises, and in equipment in case of enterprises providing or rendering services, as shown in the following table.

## **Insert Table 1 Here**

SMEs are not uniform across the globe. The way they are defined depends on the stage of economic development and the broad policy purposes for which the definition is used. The most commonly used definitions relate to either size of employment and or quantum of capital investments or fixed assets. As the process of economic development leads to changes in industrial sector shares in GDP and the contribution of sub-sectors within industry, the definition is extended to include not only manufacturing industries but all enterprises which fall within or below the defined cut off point.

Small scale units engage themselves in various kinds of manufacturing such as manufacturing of metal alloys and products, machinery, electrical equipments, chemicals, drugs, electronics and miscellaneous products. But most of the small scale units have not been able to achieve capacity utilization to the fullest extent. A very few of them have been able to achieve a capacity utilization greater than 80%, as revealed by many surveys.

Recent study conducted at Dakshina Kannada and Udupi Districts of Karnataka have indicated that more than 80 of the industrial units in the various industrial estates of the two districts are either closed or sick. The fact that the same scenario prevails throughout the country and the difference, if any, is only in degree and cannot be a consoling factor. We know that this situation is not good for the economy of the country and due to these financial institutions and the banks in the country themselves are becoming sick as it increases the non-performing assets' of industrial units and other enterprises.

The position of Sick SSI and Weak and non-viable units financed by commercial banks are not encouraging. The following table throws light on the magnitude of sickness.

### **Insert Table 2 here**

Despite several measures for the promotion of this sector, it is very disappointing to observe that its performance has not been satisfactory. The problems are many like finance, production, marketing, labour, which have resulted in under utilization of installed capacity. At the same time, power cut, lack of demand, lack of working capital are all hindering the full utilization of installed capacity.

### **Objectives of the Study**

The present study is intended to examine the capacity utilization of selected small scale units in the Udupi Districts and to find out the reasons for it. The specific objectives are:

To examine and project the existing performance level of industrial units in the study area.

To investigate into the reasons for underutilization of capacity in the small scale units of target area.

To examine the relation between the investment and capacity utilization.

To examine the relationship between the age of the unit and the capacity utilization.

to examine the relation between the background of the entrepreneur and capacity utilization

To study the current status of the small and medium scale industries

To study the industrial policy and importance of the small-scale industries.

## **Limitation of Study**

The study is not free from limitations. Some of them are likely:

Udupi district itself is not an industrialized area; hence based on this study we cannot make generalizations.

The researcher collected data from only 100 respondents, out of which only 85 units responded.

Few sample units did not maintain the books for recording their capacity utilization, production, etc. Hence collected data may be biased.

## **Review of Literature**

A number of studies on the efficiency of small and medium industries were undertaken. Dhar and Lydall, Hajra, Sandesara (1966 and 1969) and Mehta studied the relationship between size and output-capital ratio by using the data from confederation of medium industries. Their report showed positive relationship.

Bhavani (1980) conducted a detailed census of SSI units and concluded that the capital productivity of SSI units is lower than that of large scale units

suggesting efficiency differences in line with the findings of Dhar-Lydall-Sandesara.

Tambiinam T(2007) found out that the levels of productivity are higher in large enterprises (LEs) and foreign-owned enterprises than in small and medium enterprises (SMEs), partly because they have higher levels of technology capacity. He suggested that increasing the productivity of SMEs might be facilitated through improved knowledge or technology.

Business outlook survey conducted by Confederation of Indian Industries (CII) based on preliminary analysis of responses from 352 small and medium members reveals a dull scenario (June 2003). However, the small and medium industry foresees an improvement in the business situation in the coming years and expects an increase in turnover of production, profit margins, capacity utilization and exports.

According to the information collected from Small Scale Industrial Centers, Government agencies for small scale industries and some of the associations of the small scale industries, no in depth studies have been made till now on the capacity utilization of small scale industries. Under utilization of capacity may be considered as one of the problems, but neither the entrepreneurs nor the concerned authorities have taken up this issue very seriously.

Empirical studies in several countries show that SMEs are characterized by

Lower and more variable profitability (Dunlop, 1992; Cosh and Hughes, 1993; Peel and Wilson, 1996);

Lower liquidity (Gupta, 1969; Chittenden et al, 1996);

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Lower use of long-term debt (Chittenden et al., 1996; Levratto, 1997; Audretsch and Elston, 1997);

Lower leverage (Rivaud-Danset et al., 1998);

Higher short-term debt (Tamari, 1980; Cosh and Hughes, 1993; Rivaud-Danset et al., 1998).

In one of the studies conducted by Prof. Jayachandran, Narendra Kumar and Dr. Himachalam at selected small scale units of Tirupathi Industrial Estate revealed that 50% of the SMEs were utilizing 25% to 50% capacity and the remaining 50% were utilizing 50 to 75%. None of the studied units was utilizing more than 75% of plant capacity. Further it revealed that age of the unit alone is not accountable for the extent of capacity utilization. They concluded that entrepreneurial talents and problems, which confronted the unit, also influenced the level of capacity utilization in the small scale units.

From the above review, it is obvious that few research studies have been undertaken on the subject capacity underutilization in SMEs. Hence, there is a research gap necessitating further study, particularly SSI sector and the problems confronted by them. This paper throws light on the status of small and medium enterprises and their capacity utilization.

## **Research Methodology**

The present study aims at examining the status of small industries, industrial policy and capacity utilization of small industries and the reasons for not utilizing it to the fullest extent. Capacity utilization has been examined taking into account the location of the unit, industry group to which it



belonged, year of establishment, form of organization, investment in plant and machinery, the entrepreneur's background and various reasons specified by the entrepreneurs. This study is empirical in nature and it is based on the data collected with the help of questionnaire. Attempts have also been made to extract the correct information through discussion with the entrepreneurs.

Chi-square test is applied to study the association between capacity utilization and variables like location of the plant, investment, age of the unit and background of the industrialists. Besides the primary data, necessary information and data also collected through secondary sources like periodicals, reports, Government, publications of industrial association, research organization, and company documents. Documents are also collected from District Industrial Centre of Udupi and Industries Association, Manipal.

In the study, convenience sampling of 85 units were selected.

Heterogeneous sample units were selected for the study. Importance was given for the amount of investment on the units and the location as well.

## **Present Study**

There are 15 medium scale industries existing in the District. Among them printing, fishnet, granite, water gel explosives are the major industries. There are 5629 tiny and small scale industrial units registered in the District. Total amount of Rs. 218. 49 crores has been invested in these units generating employment for 34, 123 numbers.

Table reveals the number of SSI registered, the total investment and employment generation by this sector.

### **Insert Table 3 here**

Table shows the list of existing medium scale industries up to 31-3-2008.

### **Insert Table 4 here**

The District has only one industrial area and it is located at Shivally – Manipal, about 5 kms from Udupi town. There are 3 industrial estates one at Shivally, Manipal in Udupi Taluk and the others at Koteshwara in Kundapur Taluk and Karkala in Karkala Taluk.

The District has ports at Malpe, Gangolly and Hangarakatte. But these ports are not used for commercial transportation, for commercial transportation the nearest port is New Mangalore port at Mangalore. The District has the nearest aerodrome at Mangalore

### **Capacity utilization in – a sample survey conducted at Udupi District.**

The study is based on data collected from primary and secondary sources. The primary data were collected from 85 Small Scale Industrial Units situated in an around the Udupi District. Table 5 shows the Capacity Utilization-Industry Group Classification.

### **Insert Table 5 here**

Table 5 shows that out of 85-sample units, 4 units (5%) utilized up to 25% while 13 units (15%) utilized between 26 to 50% of their capacities. 39 units (46%) utilized between 51 and 75% of their capacities and the remaining 29

(34%) utilized above 75%. It can be seen that nearly 20% of the sample units were not in a position to exceed 50% of their capacities.

### **Insert Table 6 here**

Table 6 depict the capacity utilization of the units based on their location i. e. whether they are located in industrial estates, commercial area, residential area or non-residential area. Out of 55 units which were located in industrial estates 12 units (23%) used their installed capacities upto 50% only. In the case of units located in commercial area 2 out of 15 units (13%), residential areas 3 out of 9 (33%) and non residential areas all the 6 units utilizes more than 50% of their installed capacities.

### **Insert table 7 here**

An attempt has been made to examine the direct reasons for utilizing the capacity to the fullest extent. The various reasons indicated by the entrepreneurs are presented in Table 7. Inadequate market demand and inadequate working capital were equally predominant reasons. 45 out of 85 entrepreneurs stated the above reasons.

Irregular and inadequate power supply, reported by 13 entrepreneurs.

Inadequate work force (12units), 8 units facing problems from brand products, 8 entrepreneurs stated other reasons like excess tax, technological problems etc. and inadequate raw material reported by 4 entrepreneurs.

Out of 4 units which were utilizing their capacity upto 25 percent only 2 stated inadequate working capital as the reason for not utilizing their capacities while 2 units indicated inadequate market demand as the reasons.

In the case of ancillaries, mother unit not buying as per the stipulated terms was reported by few units.

Thirteen units utilized their capacity between 26 and 50 percent. Among these inadequate market demand appears to be the major problem compared to inadequate working capital.

In the third category, 39 units utilized their capacities between 51 and 75 percent. Inadequate market demand posed a big problem compared to the problem of inadequate working capital. The former was reported by 15 units whereas the latter by 5 units. Inadequate workforce and irregular and inadequate supply of power were mentioned by 5 units each and 6 units stated other reasons.

Among 29 units which were utilizing above 51 percent of their capacities on an average 5 each were facing the problems of inadequate working capital, inadequate workforce, inadequate market demand, problem of raw material supply, power cut, problems from branded products and other reasons were mentioned by three and two units respectively.

The above analysis shows that the problems vary from unit to unit. The reasons could be the different types of growing needs. The analysis indicates that units at both lowest and highest extremes largely faced the problem of finance, whereas the units at medium level mostly faced the problem of marketing.

In order of assess the impact, capacity utilisation was taken as the criterion in this study. The capacity utilisation level was divided into four categories:

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up to 25 percent, between 26 and 50 percent, between 51 and 75 percent, and above 75 percent. The capacity utilisation was examined vis a vis other variable which included the industry group to which they belonged, location of the unit, year of establishment, form of organization, investment in plant and machinery, age of the unit, background of the entrepreneur.

The analysis of the study reveals that only 20 percent of the sample units were not in a position to exceed 50 percent of their capacities. But 65 percent of the sample units were unable to reach the 75 percent of their installed capacity.

The study of Small Scale Units makes it clear that the form of organization, the area of location, investment in plant and machinery, the background of entrepreneur etc do not influence capacity utilisation. But the various reasons indicated by entrepreneurs say inadequate market demand, inadequate working capital, inadequate raw material inadequate workforce, power failure and competition from branded products were reasons for the underutilization of installed capacity.

## **SUGGESTIONS**

In order to overcome the bottlenecks faced by the small-scale units following measures are recommended.

Inadequate market demand and inadequate working capital are the major problems confronted by the small-scale units. Marketing problem includes inadequate market demand, fluctuations in demand, competition from large industrial units and etc. To solve the problem of inadequate or fluctuating market demand the Government agencies must give small entrepreneurs <https://assignbuster.com/status-and-capacity-utilization-in-small-scale-industries/>

periodical training and educate them about modern marketing, using flexible pricing, promotion, incentive and other methods to increase demand including the different uses for the same product. Management Institutions can also extend their help to the small-scale units to modernize their marketing techniques.

To solve the working capital problem it is better to take the help of professional financial experts say chartered accountants and cost accountants. As well as Institutes like Chartered Accountants or Cost Accountants and Financial Management Institutes should extend their assistance to the small-scale units.

Proper manpower planning and adequate wages and salaries can overcome inadequate workforce.

Power failure, inadequate supply of power, and load shedding must be avoided. Due to various reasons the Electricity Corporation is not able to prevent their occurrence. The concerned Governments should take interest to improve the power supply. Alternative sources of energy may be made available to the small-scale industries as a part of the National Energy Policy.

Other causes such as excessive sales tax, procedural delays and practices can be removed by streamlining the tax structure and the office methods followed.

## CONCLUSION

The cost and value of small-scale industries could benefit a large section of our country's population, if the resources and efforts of small-scale industries could be more productively used.

It is common knowledge that on the one hand surpluses generated are far below normal expectations and on the other obsolescence and industrial sickness among small scale industries threaten to become a net drain. Although the awareness of these issues is now more widespread, the problem of social and economic insecurity prevents effective measures from bringing about the change. The subject of fuller utilisation of capacity, modernization and productivity thus tend to be obscured. But the punishment for inaction will be very heavy. To avoid it the need to change now becomes imperative and unavoidable.

Lack of real consultants is adding to the problem. The so called consultants who exist in large numbers, tend to indicate every project as viable as otherwise it affects their own viability and existence. They make every project a success on paper and in reality hardly 20% of the projects register success. The practice of starting enterprise based on exemptions and subsidies is adding to the problem.

Thus a deep study of the capacity utilization in small industries is a crying need. The government policy also needs review in the interest of promoting fuller growth of small-scale units and making them viable.

In the present study an attempt has been made to examine the capacity utilisation of small-scale industries in Udupi district and the reasons for not  
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utilizing the capacity into the fuller extent. Capacity utilisation was examined taking into account the location of the unit, the industry group to which it belonged, year of establishment, form of organization, investment in plant and machinery, the entrepreneur's background and reasons indicated by the entrepreneur.

Now in this era of socio-economic transformation and favorable conditions it is the turn of small-scale industries to rise to the occasion and tell the society that they are capable of producing results.