CHAPTER-I

INTRODUCTION AND RESEARCH METHODOLOGY
Introduction

The Industrial sector in India over the past 60 years has made a significant contribution towards building a strong and stable national economy. It is the second largest employment source in the country only after the agriculture sector. Owing to the limitations of the agricultural sector to contribute adequately to the economy, the industrial sector has acquired greater importance in our country. Realising the importance of the industrial sector for economic development, our planners have aimed at accelerating industrial development through rapid industrialization by exploitation and effective utilization of the available rich natural and physical resources of the land. Moreover, the development of human resource has also gained lot of importance since there can be development of any kind without human resources fully developed. Any negligence of the human factor would only enfeeble the economic prosperity of the country. Consequently, the industrial policies of the government and the successive Five Year plans over the years have reiterated the government’s intention to stimulate and promote the human factor in industrial development. Thus, the entrepreneur has gained importance and also become the nerve centre of all economic activity.

In our present day economy, Finance is defined as the provision of money at the time when it is required. Every enterprise, whether big, medium or small, needs finance to carry on its operations and to achieve its targets. In fact, Finance is so indispensable today that it is rightly regarded as the lifeblood of an enterprise. Without adequate Finance, no enterprise can possibly hope to accomplish its objectives. Therefore, financial performance has become a necessary part of the any study of economic activity. Financial analysis is the process of identifying the financial strength and weaknesses of the firm by establishing a proper relationship between the items of the balance sheet, profit and loss account and the cash flow statement.

Concept of Financial Analysis

Financial statements are prepared primarily for decision-making. They are essential to set the framework of managerial decisions. But the information provided
in the financial statements is not an end in itself as no meaningful conclusions can be
drawn from these statements alone. However, the information provided in the
financial statements is of immense use in making decisions through an analysis and
interpretation of them.

The term ‘financial analysis’, also known as ‘analysis and interpretation of
financial statements’, refers to the process of determining the financial strengths and
weaknesses of the firm by establishing a strategic relationship between the items of
the balance sheet, profit and loss account and other operative data. In the words of
Myers, “Financial statement analysis is largely a study of relationship among the
various financial factors in a business as disclosed by a single set of statements, and
a study of the trend of these factors as shown in a series of statements.” In the
words of Anthony, “Financial statements, essentially, are interim reports, presented
annually and reflect a division of the life of an enterprise into more or less arbitrary
accounting period – more frequently a year.

Objectives of Financial Statements

Financial statements are the source of information on the basis of which
conclusions are drawn about the profitability and financial position of a concern.
They are the chief means employed by firms to present their financial situation to
the owners, creditors and the general public. The Accounting Principles Board of
America (APB) states the following as the objectives of financial statements:

i) To provide reliable financial information about economic resources and
obligations of a business firm,

ii) To provide other needed information about changes in such economic
resources and obligations,

iii) To provide reliable information about changes in net resources (resources
less obligations) rising out of business activities,

iv) To provide financial information that assists in estimating the earning
potentials of business, and
v) To disclose, to the extent possible, other information related to the financial statements that is relevant to the needs of the users of these statements.

Financial analysis (also referred to as financial statement analysis or accounting analysis) refers to an assessment of the viability, stability and profitability of a business, sub-business or project. It is performed by professionals who prepare reports using ratios that make use of information taken from financial statements and other reports. These reports are usually presented to top managements as one of their bases in making business decisions. Based on these reports, a management may:

i) Continue or discontinue its main operation or part of its business;

ii) Make or purchase certain materials in the manufacture of its product;

iii) Acquire or rent/lease certain machineries and equipment in the production of its goods;

iv) Issue stocks or negotiate for a bank loan to increase its working capital;

v) Make decisions regarding investing or lending capital;

vi) Other decisions that allow management to make an informed selection on various alternatives in the conduct of its business.

Financial analyst - Goals

Financial analysts often assess the firm's:

1. Profitability - its ability to earn income and sustain growth in both short-term and long-term. A company's degree of profitability is usually based on the income statement, which reports on the company's results of operations;

2. Solvency - its ability to pay its obligation to creditors and other third parties in the long-term;

3. Liquidity - its ability to maintain positive cash flow, while satisfying immediate obligations;

Both 2 and 3 are based on the company's balance sheet, which indicates the financial condition of a business as of a given point of time.
4. Stability - the firm's ability to remain in business in the long run, without having to sustain significant losses in the conduct of its business. Assessing a company's stability requires the use of the income statement and the balance sheet, as well as other financial and non-financial indicators.

The purpose of financial analysis is to diagnose the information contained in financial statements so as to judge the profitability and financial soundness of the firm. Just like a doctor who examines his patient by recording his body temperature, blood pressure, etc, before making his conclusion regarding the illness and before treating him, a financial analyst analyses the financial statements with various tools of analysis before commenting upon the financial health or weaknesses of an enterprise. Such analysis and interpretation of financial statements are essential to bring out the mystery behind the figures in financial statements. Financial statements analysis is an attempt to determine the significance and meaning of the financial statement data so that forecast may be made of the future earnings, ability to pay interest and debt maturities (both current and long-term) and profitability of a sound dividend policy.

Types of Financial Analysis:

Financial Analysis can be classified into different categories depending upon
(i) the material used and (ii) the modus operandi of Analysis

Figure 1.1
Types of Financial Analysis

![Diagram of Types of Financial Analysis](image-url)
According to material used, Financial Analysis can be of two types:

a) External Analysis, and

b) Internal Analysis

a) **External Analysis**: This analysis is done by those who are outsiders to the business. Such as investors, credit agencies, government agencies and other creditors who have no access to the internal records of the company. These persons mainly depend upon the published financial statements. Their analysis serves only a limited purpose.

b) **Internal Analysis**: This analysis is done by those who have access to the books of account and other information related to the business. Such an analysis can, therefore, be performed by executives and employees of the organization as well as government agencies which have statutory powers vested in them.

ii) **Analysis on the basis of modus operandi**:

According to the method of operation followed in analysis, financial analysis can also be of two types: a) Horizontal analysis and b) Vertical analysis.

a) **Horizontal Analysis**:

Horizontal Analysis refers to the comparing year-wise the financial data of a company for several years. The current year's figures are compared with those of standard or base year. A base year is a year chosen as the beginning point. This type of analysis is also called Dynamic analysis as it is based on the data from year to year rather than on the data of any one year.

b) **Vertical Analysis**:

Vertical Analysis refers to the study of relationship of the various items in the financial statements of one accounting period. In these types of analysis the figures from the financial statement of a year are compared with a base selected from the same year's statement. It is also known as 'Static Analysis'. Common-size financial statements and financial ratios are the two tools employed in vertical
analysis. Since vertical analysis considers data for one time period only, it is not very conducive to a proper analysis of financial statements. However, it may be used along with horizontal analysis to make it more effective analysis to make it more effective and meaningful.

Devices of Financial Analysis:

Analysis and interpretation of financial statements are used to determine the financial position and results of operations as well. A number of methods or devices are used to study the relationship between different statements. Those devices which clearly analyse the position of the enterprise are made use of.

The following methods are generally used;


1) Comparative Statements:

Comparative statements are statements of the financial position at different periods of time. The elements of financial position are shown in a comparative form so as to give an idea of the financial position during two or more periods. Any statement prepared in a comparative form will be covered in comparative statements. Generally two financial statements (Balance Sheet and Income Statement) are prepared in a comparative form for financial analysis purposes. Not only the comparison of the figures of two periods but also be relationship between the balance sheet and income statement enables an in-depth study of financial position and operative results.

The comparative statements may show:

(i) Absolute figures (rupee amounts)

(ii) Changes in absolute figures i.e., increase or decrease in absolute figures

(iii) Absolute data in terms of percentages

(iv) Increase or decrease in terms of percentages
The analyst is able to draw useful conclusion when the figures are given in a comparative position. The figures of sales for a quarter, half-year or one year may tell only the present position of sales efforts. When the sales figures of previous periods are given along with the figures of current periods then the analyst will be able to study the trends of sales over different periods of time. Similarly, comparative figures will indicate the trend and direction of financial position and operating results.

The financial data will be comparative only when the same accounting principles are used in preparing these statements. In case of any deviation in the use of accounting principles this fact must be mentioned at the foot of financial statements and the analyst should be careful in using these statements. The two comparative statements are (i) Balance sheet, and (ii) Income statement.

(i) Comparative Balance sheet

The comparative balance sheet analysis is the study of the trend of the same items, group of items and computed items in two or more balance sheets of the same business enterprise on different dates. The changes in periodic balance sheet items reflect the conduct of a business. The changes can be observed by comparison of the balance sheet at the beginning and at the end of a period and these changes can help in forming an opinion about the progress of an enterprise. The comparative balance sheet has two columns for the data of original balance sheets. A third column is used to show the increase in figures. A fourth column may be added for giving percentages of increases or decreases.

While interpreting the comparative balance sheet the interpreter is expected to study the following aspects: (i) Current financial position and liquidity position (ii) Long – term financial position (iii) Profitability of the concern

(ii) Comparative Income Statement

The Income Statement gives the results of the operation of a business. The comparative income statement gives an idea of the progress of a business over a period of time. The changes in absolute data in money values and percentages can be determined to analyse the profitability of the business. Like the comparative balance sheet, the income statement also has for columns. The first two columns give figures of various items for two years. The third and fourth columns are used to show the increase or decrease in figures in absolute amounts and percentages respectively.
The analysis and interpretation of the income statement involve the following steps:

1) The increase or decrease in sales should be compared with the increase or decrease in the cost of goods sold. An increase in sales will not always mean an increase in profit. The profitability will improve if the increase in sales is more than the increase in the cost of goods sold. The amount of gross profit should be studied in the first step.

2) The second step of analysis should be the study of operational profits. The operating expenses such as office and administrative expenses, selling and distribution expenses should be deducted from the gross profit to find the operating profits. An increase in the operating profit will result from the increase in the sales position and control of operating expenses. A decrease in the operating profit may be due to an increase or decrease in the operating expense. Some expenses may increase due to the expansion of business activities while others may go up due to managerial inefficiency.

3) The increase or decrease in net profit will give an idea about the overall profitability of the concern. Non operating expenses such as interest paid, losses from sale of assets, writing off of deferred expenses, payment of tax, etc, decrease the fire of operating profit. When all non-operating expenses are deducted from the operational profit, we get a figure of the net profit.

4) An opinion should be formed about the profitability of the concern and it should be given at the end. It should be mentioned whether the overall profitability is good or not.

2) Trend Analysis

The Financial statements may be analysed by computing the trends of series of information. This method determines the direction upwards or downwards and involves the computation of the percentage relationship that each statement item bears to the same item in the base year. The information for a number of years is taken up and one year, generally the first year, is taken as the base year. The figures of the base year are taken as 100 and trend ratios for the other years are calculated on the basis of the base year. The analyst is able to see the trend of figures, whether upward or downward.
3) Common-Size Statement

Common-size statements, balance sheet and income statement are shown in analytical percentages. The figures are shown as percentages of total assets, total liabilities and total sales. The total assets are taken as 100 and different assets are expressed as a percentage of the total. Similarly, various liabilities are taken as a part of the total liabilities. These statements are also known as component percentage or 100 percent statements because every individual item is stated as a percentage of the total 100. The analyst is able to assess the figures in relation to the total values.

(I) Common-size Balance sheet

A statement in which balance sheet items are expressed as the ratio of each asset to total assets and the ratio of each liability is expressed as a ratio of total liabilities is called common size balance sheet.

(lI) Common-size Income Statement

The items in an income statement can be shown as percentages of sales to show the relation of each item to the sales. A significant relationship can be established between the items of income statement and volume of sales. The increase in sales will certainly increase selling expenses and not administrative or financial expenses. In case the volume of sales increases to a considerable extent, the administrative and financial expenses may go up. In case the sales declining, the selling expenses should be reduced at once. So a relation is established between sales and other items in the income statement and this relationship is helpful in evaluating the operational activities of the enterprise.

4) Funds Flow Statement

The funds flow statement is a statement which shows the movement of funds and is a report of the financial operations of the business undertaking. It indicates various means by which funds were obtained during a particular period and the ways in which these funds were employed. In simple words, it is a statement of sources and applications of funds.
The Funds flow statement is a method by which we study changes in the financial position of a business enterprise between the beginning and ending financial statements dates. Hence, the funds flow statement is prepared by comparing two balance sheets and with the help of such other information derived from the accounts as may be needed. Broadly speaking, the preparation of funds flow statement consists of two parts:

1. Statement or Schedule of changes in the working capital

2. Statement of Sources and Application of Funds.

5) Cash Flow Statement

Cash is very important for the entire economic life of a business enterprise. A firm needs cash to make payments to its suppliers, to incur day-to-day expenses and to pay salaries, wages, interest and dividends etc. In fact, cash is the lifeblood of a business enterprise. It is very essential for a business to maintain an adequate balance of cash. The cash flow statement is "A statement of changes in the financial position of firm on cash basis". It shows the impact of various transactions on the cash position of a firm. It is prepared with the help of financial statements, i.e balance sheet and profit and loss account and some additional information. The statement starts with the opening balance of cash and balance at bank, all the inflows of cash are added to the opening balance and the outflows of cash are deducted from the total. The balance, i.e., opening balance of cash and bank balance plus inflows of cash minus out flows of cash is reconciled with the closing balance of cash.

6) Ratio Analysis

The Ratio analysis is one of the most powerful tools of financial analysis. It is the process of establishing and interpreting various ratios (quantitative relationship between figures and groups of figures). It is with the help of ratios that the financial statements can be analysed more clearly and decisions made from such analysis. "A ratio is a simple arithmetical expression of the relationship of one number to another". It may be defined as the indicated quotient of two mathematical expressions. Ratio analysis is a technique of analysis and interpretation of financial statements. However, it is not an end in itself, but only a means of understanding better the financial strengths and weaknesses of a firm. With the help of Ratios, one can determine:
i) The ability of the firm to meet its current obligations

ii) The extent to which the firm has used its long-term solvency by borrowing funds;

iii) the efficiency with which the firm is utilizing its assets in generating sales revenue, and iv) the overall operating efficiency and performance of the firm.

7) Cost-Volume Profit Analysis (CVP analysis)

The Cost-Volume Profit Analysis is a technique for studying the relationship between cost, volume and profit. The profits of an undertaking depend upon a large number of factors. But the most important of these factors are the cost of manufacture, volume of sales and the selling prices of the products. The CVP relationship is an important tool used for planning the profit of a business. As the three factors of CVP analysis i.e., costs, volume and profits are interconnected and interdependent. Their relationship is of immense utility to management as it assists in profit planning, cost control and decision making.

To illustrate, profit depends upon sales, selling price to a large extent depends upon cost and cost depends upon the volume of production as it is only the variable cost that varies directly with production, where as the fixed cost remains fixed regardless of the volume produced. In the CVP analysis an attempt is made to analyse the relationship between the variations in cost with the variations in volume.

Uses of Financial Analysis:

As financial analysis is the process of identifying the financial strength and weaknesses of the firm by properly establishing relationships between the items of the balance sheet and profit and loss account, it can be undertaken by the management of the firm, or by parties outside the firm, viz., owners, creditors, investors and others. The nature of analysis differs depending on the purpose of the analyst.

i) Trade Creditors:

Trade creditors are interested in a firm's ability to meet their claims over a very short period of time. Their analysis will, therefore, be confined to the evaluation of the firm's liquidity position.
ii) Suppliers' of long term debt:

On the other hand suppliers of long term debt are concerned with the firm's long term solvency and survival. They analyse the firm's profitability over time, its ability to generate cash to be able to pay interest and repay principal, and the relationship between the various sources of funds (Capital structure relationship). Long term creditors analyse the historical financial statements of a firm but they place more emphasis on the firm's projected, or pro-forma financial statements to analyse out its future solvency and profitability.

iii) Investors:

Investors, who have invested their money in the firm's shares, are most concerned about the firm's earnings. They restore confidence in those firms that show steady growth in earnings. As such, they concentrate on the analysis of the firm's present and future profitability. They are also interested in the firm's financial structure to the extent that it influences the firm's earnings ability and risk.

iv) Management:

The management of a firm would be interested in every aspect of the financial analysis. It is its overall responsibility to see that the resources of the firm are used most effectively and efficiently and that the firm's financial condition is sound.

Limitations of Financial Analysis:

Financial analysis no doubt, is a powerful mechanism of determining, the financial strengths and weaknesses of a firm. But it has certain limitations of which one should be aware. It is based on the information available in the financial statements. It has also to be careful about the impact of price level changes, window-dressing of financial statements, changes in the accounting policies of a firm, accounting concepts and conventions, and personal judgement, etc. The following are of some of the important limitations of financial analysis:

i) It is only a study of interim reports,

ii) It is based upon only monetary information and non-mandatory factors are ignored,
iii) It does not consider the changes in price levels,

iv) As the financial statements are prepared on the basis of a going concern, they do not give the exact financial position. Thus the accounting concepts and conventions cause a serious limitation to financial analysis,

v) Changes in the accounting procedure by a firm may often make financial analysis misleading,

vi) Analysis is only a means and not an end in itself. The analyst has to make interpretation and draw his own conclusions. Different people may interpret the same analysis in different ways.

Micro, Small and Medium Enterprises (MSME) Development Act, 2006

The Micro, Small and Medium Enterprises (MSME) sector has been recognised as an engine of growth all over the world. Many countries have established a SME Development Agencies as the nodal agencies to coordinate and oversee all Government interventions in respect of the development of this sector. In India, the term Medium establishment has for the first time been defined in terms of a separate Act, governing the promotion and development of Micro, Small and Medium Enterprises (MSME). This came into force from 2nd October, 2006.

The Office of the Development Commissioner of Small Scale Industries (SSI) was established in 1954 in India on the basis of the recommendations of Ford Foundation. Over the years, it has evolved into an agency for advocacy, hand holding and facilitation for the small industries sector. It has over 70 offices and 21 autonomous bodies under its management. These autonomous bodies include Tool Rooms, Training Institutions and Project-cum-Process Development Centers. The Office of the Development Commissioner (MSME) provides a wide spectrum of services to the Micro, Small and Medium Industrial sector. Such as facilities for testing, toolmenting, training for entrepreneurship development, preparation of project and product profiles, technical and managerial consultancy, assistance for exports, pollution and energy audits etc. The Office (MSME) provides economic information services and advises the Government in policy formulation for the promotion and development of the SSI. The field offices also work as effective links between the Central and the State Governments.
The MSME Act aims at facilitating the promotion and development of Micro, Small and Medium Enterprises as well as ensuring their competitiveness and smooth flow of credit to them as well as minimizing instances of sickness among them. It empowers the Central Government to notify programmes, guidelines and instructions for the promotion and growth of Micro, Small and Medium enterprises. Under the Act, the Central Government and the State governments may construct preference policies in respect of procurement of goods and services provided by such enterprises. In brief, the basic objective is to ensure the overall development of Micro, Small and Medium Enterprises.

The definitions given by the Act are as follows:

(a) For manufacturing enterprises -

(i) A micro enterprise is one where the investment in plant and machinery does not exceed Rs.25 lakh;

(ii) A small enterprise is one where the investment in plant and machinery is more than Rs.25 lakh but does not exceed Rs.5 crore:

(iii) A medium enterprise is one where the investment in plant and machinery is more than Rs.5 crore but does not exceed Rs.10 crore

(b) For Servicing enterprises -

(i) A micro enterprise is one where the investment in plant and machinery does not exceed Rs.10 lakh;

(ii) A small enterprise is one where the investment in plant and machinery is more than Rs.10 lakh but does not exceed Rs.2 crore:

(iii) A medium enterprise is one where the investment in plant and machinery is more than Rs.2 crore but does not exceed Rs.5 crore

The global pharmaceutical industry is a multinational industry. It is highly regulated, capital intensive, and is driven by large research and development expenditures. The industry is primarily privately owned and is technologically sophisticated. The SMEs play an important role in the Indian pharma sector. Around 5000 SMEs produce 40 per cent of Rs. 70000 crores worth medicines in India. They
are the largest employer in the pharma sector. For a long time, these SMEs have been providing of quality at very cheap prices medicines in abundance. Because of its competitive nature the multinational pharma companies are intolerant of the small pharma, and thus hold out a threat for its survival. This not out of place to mention here itself that governments which knows the value of the small pharma sector should take steps constantly to protect and sustain it.

It is a matter of satisfaction that the Indian pharmaceutical industry today is in the front rank of India’s science-based industries with wide ranging capabilities in the complex field of manufacture and technology. A highly organized sector, the Indian pharma industry is estimated to be worth $4.5 billion, growing at about 8 to 9 per cent annually. It ranks very high in the third world, in terms of technology, quality and range of medicines manufactured. From simple headache pills to sophisticated antibiotics and complex cardiac compounds, almost every type of medicine is now made indigenously.

In Andhra Pradesh is capital city, Hyderabad, and the fifth largest city in India, is the hub of pharmaceutical and bulk drugs industry. Hyderabad has achieved excellence in the fields of pharmaceuticals, healthcare. Andhra Pradesh’s pharmaceuticals sector is internationally known for its skills in chemical synthesis and process engineering on the one hand, and its commitment to the invention of new molecules on the other.

Since Independence in 1947, a significant feature of the Indian economy has been the rapid growth of the small industry sector which has been aided among other things, by specific and general policy initiatives (e.g. Industrial Policy Resolutions). The Small and Medium Enterprises have been playing an extraordinarily important role as nucleus for regional economic development. They have contributed considerably improving the quality of life by providing the local communities with goods and services and significantly to the validity of Indian economy. But as a consequence of globalization of the economy in India, complied with the WTO regime, the Indian SMEs have been passing through a transnational period. The stress and pressure exerted as them has become heavy, challenging their very survival. The larger companies and enterprises seem to them by what looks like commercial Darwinism, the stronger devouring the weaker and smaller. Owing to
increasing competition on account of globalization of the Indian economy, the size of the Small and Medium enterprises and the level of technology employed by them have assumed critical significance for their global competitiveness. Several policy initiatives have been taken during the years to address the problems faced by the sector, which mainly relate to access to timely and adequate credit, high cost of loans, delayed payment by large scale buyers, technology obsolescence, infrastructure bottlenecks, marketing constraints, working capital requirement, sickness and a plethora of rules and regulations.

In the competitive environment, the weaknesses of pharmaceutical small and medium enterprises (SMEs) in their endeavour towards trans-nationalization and exports surface themselves. These include: lack of expertise, training and finance for technological up-gradation and adoption of good manufacturing practices (GMP) by the SMEs to meet global quality standards; limited exposure to and expertise on Intellectual Property Rights (IPR) issues; limited adoption of Information Technology (IT) techniques in production and processes; low or negligible R&D expenditure which affects the ability of SMEs to offer innovative solutions; and the inability of the SMEs to access finance on easy terms for import of capital goods and undertaking advertising and marketing activities.

Most of the small and medium enterprises in the pharmaceutical segment operate in the local market, and mainly manufacture formulations. To a great extent, the survival of these units at present would depend on how well and quickly they are able to adapt to the changing business scenario.

Review of Literature

The present study of “Financial Performance of Small and Medium Enterprises (SMEs) – with particular reference to the pharmaceutical industry in Andhra Pradesh” is concerned with the various issues relating to the financial performance of the SMEs in the pharma industry. The current body of knowledge in the field of pharma of the SMEs is still under development. There is a need to develop in detail an understanding of the financial performance strategies of the SMEs in the pharmaceutical industry and their appropriateness in different situations.
There are some studies which focus on the financial performance of small scale industries and the SMEs. But there does not seem to have been study of the financial performance of the pharma units among the SMEs, particularly in Andhra Pradesh. The present study is a modest attempt to fill this gap.

H.H. Pathak (1972)\(^7\) In his article considers briefly 12 industrial units with a view to evaluating the performance and problems of small-scale industries during 1969-1971. He studies the problems of the select SSIs at three different stages namely, inception, operation and expansion. He observes that factors like contacts, education and finance have played an important role and the problems at the stage of inception received relatively more attention than the problems of the remaining two stages.

P.D Malgawakar (1973)\(^8\) in his study the “Problems of Small Industry in Andhra Pradesh” has found the lack of infrastructure as a general problem. The industrial estates by themselves could not overcome the location disadvantages. The infrastructure facilities were either very weak or non-existent in the rural areas. In urban areas with the necessary industrial climate and infrastructure facilities, the growth of industries was relatively faster.

T.Subbi Reddy and P.L.N.S.S.G.K.Moorthy (1979)\(^9\) in their article analysed the issue of capacity utilization by the small-scale sector in the industrial estate of Ananthapur district of Andhra Pradesh. They identified marketing, financial, labour and managerial problems as the prime causes for the under-utilization of the capacity. They recommend and the regulation of entry of new firms and marketing of produce by the Government to improve their capacity.

R.K Sharma (1982)\(^10\) in his book Industrial Development of Andhra Pradesh – A Regional Analysis has made a study of the growth and problems of the small-scale sector in Andhra Pradesh. He observes that the backward districts of the state improved their relative position in terms of units’ employment and capital during 1966-75. But the majority of the small units confronted the problems of raw materials and finance.

Ramakrishnan Sarma’s (1982)\(^11\) book-length study, Industrial development of Andhra Pradesh, is thoughtful and authoritative. He examines the
role of different state level institutions including Andhra Pradesh State Financial Corporation in the Industrial Development of the state. The conclusions emerging from his study mainly include inadequate assistance to the backward districts, low disbursement ration in case of backward districts and financial crisis of many of the enlisted in regard to their working capital.

R. Natarajan’s (1983)\textsuperscript{12} in his doctoral dissertation is a commendable study on “Institutional Finance for Small Scale Industries in Andhra Pradesh”. He has analyzed the role of the APSFC as a financial institution in financing small-scale industries in the state. He recommends that in order to check the diversion of funds, keeping in view the interest differentials between banks and the APSFC, post-disbursement follow-up and supervision of the loans by the APSFC is warranted. In view of the elaborate formalities, which are difficult to be complied with by the assisted units, it is also suggested that the policy-makers of the APSFC may consider the possibility of reducing the procedural formalities in the case of the SSI units.

T. Sathyanarayana (1986)\textsuperscript{13} in his doctoral thesis examines the “Financing of Small Scale Industries with special reference to Andhra Pradesh State Financial Corporation” during two years 1974-75 and 1983-84. This is a worth-mentioning Study. Primarily, his is a macro-economic study of the APSFC for its role as a major source of industrial finance in Andhra Pradesh. He concludes that assistance or any incentive offered to individual industries cannot be properly evaluated, if the industry is de-linked from the best within the cluster.

V. Lakshmana Rao (1986)\textsuperscript{14} in his book Industrial Entrepreneurship in India, studies about fifty-one entrepreneurs of Krishna and Gunter districts in Andhra Pradesh, to find out how far the programmes and policies of the government have fostered industrial entrepreneurship. He is of the view that the government schemes have certainly given a boost to entrepreneurship in Andhra Pradesh.

Pannalal (1994)\textsuperscript{15} in his article briefly takes into account 2,822 Small-scale industries in 3 industrial estates of Andhra Pradesh, which are spread over the three regions of the state. He finds that 62.60 per cent of the engineering industries could be regarded as an important segment of activity in the promotion and dispersion of small-scale industries. As such these industries deserve to be accorded a special emphasis among the entrepreneurs intending to set-up small-scale units. Of the different patterns of entrepreneurship in the industries considered the most popular and successful.
M.Lakshmi Narasaish and N.Anuradha (1999) in their study have analyzed the growth and performance of small-scale industries in 7 industrial estates in Ananthapur district of Andhra Pradesh and identified the problems of small-scale industries. Shortage of necessary industrial inputs, the marketing of products, paucity of funds, lack of working capacity, lack of technical know-how, non-availability of trained and skilled workers, power shortage, etc., are identified as the basic problems encountered by the small-scale industries. The study suggests the establishment of raw material depot, an industrial training institute and provision of better infrastructure facilities in the industrial estates.

Mahalingam (2002) in his article observes that in order to encourage the SSIs which are handicapped by inadequate availability of finance, the Government should allocate higher capital assistance, which will enable them to widen the range and scope of production. Venture capital companies should be promoted in a big way.

Raj Kumari's (2002) study entitled "Working Capital Management in Indian Drugs and Pharmaceuticals Limited" probes various problems of Working capital management of Indian Drugs and Pharmaceuticals Limited (IDPL). Her conclusion is that an efficient working capital management is necessary for achieving both liquidity and profitability of a firm. A poor and inefficient management leading to a tie-up of funds in idle assets reduces the liquidity and profitability of a company.

R.Padmaja (2004) in her article points that one Indian Companies need to attain the right product-mix for sustained future growth. Core competencies will play an important role in determining the future of many Indian Pharmaceutical Companies in the post product-patent regime after 2005.

P.Kameswari and D.Raghunatha Reddy (2004) in their article point one that an efficient working capital management is necessary for achieving both the liquidity and profitability of a firm. A reputed pharmaceutical company, the Cipla Limited, has been selected for a case study of working capital management during 1998-2003. The current ratio, quick ratio, net working capital position, and the working capital turnover ratio of Cipla have been found to be within or slightly fluctuating around the Indian Pharmaceutical Industry Standards, indicating an overall efficiency in the management of the company's working capital.
Vipin Agarwal (2004) in his article contends that all over the world efforts are being made to encourage the economic growth. But growth with the high employment and rising living standards needs some creative efforts. As people pursue new directions in business science, and arts, they develop innovations and improvements that drive the economy forward. Intellectual property right – patents and copyrights- is the clearest example of that.

Berry (2004) "The Pharmaceutical Regulatory Process (Drugs and the Pharmaceutical Sciences 144)" provides an in-depth coverage of the procedures utilized by pharmaceutical companies for regulatory compliance, it describes the history and development of regulations, standards, and guidelines that affect pharmaceutical product approval and commercial sale in the United States-standing alone as the only authoritative guide to address the complex web of regulatory requirements, application processes, and quality control issues influencing the pharmaceutical industry.

V Darling Selvi (2005) in her article "Financial performance of pharma company: A case study (TTK Pharma company) observed that a company is able to increase the profitability, lack of efficiency in controlling expenditure and lowering the stock on the part of the management resulted in a negative trend of activities. It is suggested in the study that, proper planning with adequate investment and the speedy recovery of bad debt, will definitely help the concern to have a steady progress.

Nustmed. (2005) "Active Pharmaceutical Ingredients: Development, Manufacturing, and Regulation (Drugs and the Pharmaceutical Sciences 151) ", Focuses on the three most critical components that successfully bring an API to market-process development, manufacturing, and governmental regulation and approval. It serves as a step-by-step guide to the planning and clear understanding of the bulk manufacturing of APIs. It offers current and timely discussions of the process, development cycle, design engineering, the approval process, quality control and assurance, and validation, as well as plant manufacturing activities including materials management, maintenance, and safety. Filling a gap in the literature, this guide covers all the essential information required to effectively plan and execute manufacturing of the APIs.
R.K Agrawal and Seeman Agrawal (2005)\textsuperscript{25} in their article "Trips and their impact on Indian Pharmaceutical Industries" point out the emerging patent regime throws up both challenges and opportunities for Indian Industries. In the new environment the challenges will be to identify potential opportunities for technology development and commercialization and make adequate investment in domestic R & D to exploit these opportunities.

K.A Ganjre (2005)\textsuperscript{26} in his article "Critical evaluation of Recruitment, selection and training in Pharmaceutical marketing in India" agrees that as competition becomes more severe day-by day the taste of field persons becomes tougher. There is growing need to redefine his job profile from a media of communicating to effective personally built to en-cash market potential.

Suresh K.Chadha, Ramanjit Johal and Keshav Malhotra (2007)\textsuperscript{27} in their article develop a knowledge management model to fit the SMEs in the pharma sector, to study the current state of Knowledge Management practices in the selected SMEs and suggest measures to leverage better knowledge management practices in the SMEs in the pharma sector for enhanced global competitiveness.

Sudha AkkiRaju (2007)\textsuperscript{28} in her doctoral dissertation "Supply chain management practices in Pharmaceutical companies - A study ", makes a study of the supply chain as all the activities involved in delivering a product from raw material to delivery to the customer and the information systems necessary to monitor all of the activities, which involves sourcing of raw material, manufacturing and assembly, warehousing and inventory and order to entry management in pharmaceutical companies.

Sudershan Kuntluru (2008)\textsuperscript{29} in his doctoral dissertation "Foreign Direct Investment and its impact on the performance of Pharmaceutical Industry in India, explains the literature pertaining to the impact of FDI on the export performance of firms. One of the features of the FDI is access to export markets and in turn it is expected that it will increase the host country firm's exposure to international trade as compared to the pharmaceutical industry in India.

Rajesh Kumar Singh in his article Indian Pharmaceutical Industry: Changing Business Dynamics\textsuperscript{30} suggests that Indian companies will have to shift their focus on to western generic markets. The low development costs will
encourage global pharma companies to set up bases in India. India will be a preferred destination for clinical testing. Thrust towards basic research will be the key driver of growth. The generic manufacturers can only succeed provided they have cost-effective manufacturing processes and their plants are approved by the USFDA. Foreign companies which have 100% subsidiary units in India will get new technology, which, in turn, will help the industry. The lifestyle therapeutic segment will contribute to growth in the years to come. In future, contract research and manufacturing will shift to India.

Srikanth Gandhir in his “The Indian Pharmaceutical Industry: Opportunities and Challenges” presents a case study which helps readers to understand the applications of article 6, article 7, article 8, article 9 and article 10. The Indian pharmaceutical companies survived on the drugs that were manufactured by reverse engineering. The growth of the industry was dependent on the generic market. There is an opportunity now in the global generics market, as many block busters are going off patent. The Indian companies should move up the value chain. Foreign companies will outsource bulk drugs and formulations to Indian companies. Moreover, the Indian companies will be engaged in Contract Research and Contract Manufacturing.

Jaya Israni in her article “Indian Pharma: The Road Ahead” points out that the new WTO rules with effect from January 2005 have threatened India’s position in the global pharma industry, as the product patent laws are applicable, which will challenge the generic based growth in India. In order to manufacture new products for their survival, the Indian companies will have to invest in Research and Development. As the number of drugs will be going off patent in the next ten years, the global generic market will certainly offer an opportunity for Indian companies.

Krishna Kum in his article “Innovation in Indian Pharma: the Key to Success” describes innovation in the Indian pharma sector, growth potential, strategic product lines, innovative practices and effect of patent changes. The four major areas of product innovation and creation are medicines and medical devices, Vaccines and prophylactics, diagnostics and laboratory investigations and therapeutics.
Statement of the Problem

The foregoing 'Review of literature' shows that there have been few or no studies at all of the financial performance of the SMEs and those particularly in the Pharmaceutical sector in Andhra Pradesh. And hence the present undertaking which is concerned with a study of the Small and Medium Enterprises (SMEs) in general and the pharmaceutical units among them in particular in this state may be regarded as something different from other academic studies in the field. It may not be farfetched to say that it indicates a necessary point of departure. The present study considers in detail the state of affairs in the SMEs sector chiefly as scaffolding for the detailed enquiry into the pharmaceutical units of Andhra Pradesh, which are its focus. More particularly it is preoccupied with their financial performance and the many challenges and problems they encounter in fulfilling their targets. The paramount importance and significance of all the units under the SMEs sector, their contribution to the growth, development, and stability of Indian economy in general, their significant role as nucleuses to regional economic development, and their contribution to the quality of life in the places and region where they are located by providing people employment opportunities, goods and services, have all been fully recognized and acknowledged. A later chapter in the present study dwells on them further.

In Andhra Pradesh, Hyderabad its capital city and the fifth largest city in India, is at present the hub of pharmaceutical and bulk drugs industry. It has the reputation of having achieved excellence in this field and healthcare. The Andhra Pradesh pharmaceutical sector is internationally known for its skills and chemical synthesis and process engineering and its commitment to discovery of new molecules. There are in Hyderabad in all about 215 pharmaceutical industries of which 17 are large, 75 medium and 123 small. Of the pharma industries 198 have been categorized as Small and Medium. As a consequence of the globalization and liberalization of Indian economy, and abetted by the WTO regime all of which have impacted the SMEs, these units, the pharma units in particular are passing through a transitional period. Owing to increasing competition, thanks to globalization of the economy, the size of the pharmaceutical enterprises and the level of their present technology to have become very critical. As pointed out already several policy
measures have been taken by the powers that be in recent years to solve the problems faced by this sector, such as finding, timely and adequate credit, high cost of loan, delayed payment by large-scale buyers, use of obsolete or obsolescent technology, infrastructure bottlenecks, marketing constraints, working capital requirement, sickness etc, and to cap them all rules and regulation in excess of requirement which are a hindrance rather than help. There are other problems resulting from necessary trans-nationalization and the necessity to export. They do not have the necessary expertise, training and finance to upgrade their technology, to adopt such competent manufacturing practices that can satisfy global standards, the pharma units in particular among the SMEs generally operate in the local markets and manufacture mainly tried formulation. Their survival is dependent on how well and how soon they are able to adopt themselves to the fast changing global business situation.

Objectives

The present study focused as it is specifically on the Small and Medium Enterprises in the pharmaceuticals industry of Andhra Pradesh, and their financial performance, has the following objectives:

i. To review the policies and programmes of the government and the Organization structure of the Small and Medium Enterprises (SME) in India.

ii. To examine the policy measures of the SME’s in the pharmaceutical industry of Andhra Pradesh.

iii. To study the efficiency of working capital management in sample units.

iv. To examine the capital structure management in sample units, and

v. To analyse the financial problems of pharmaceutical units in Andhra Pradesh and to suggest feasible ways and measures to overcome the problems they confront in their performance and enable them to tone up their overall performance.
Methodology

The present analytical study of the financial performance of select pharmaceutical enterprises among the Small and Medium Enterprises in Andhra Pradesh adopts the well-tested and established methodology of inquiry. The majority of pharmaceutical industries big, medium and small in this state are situated in and around Hyderabad city. Of them 198 units are categorized under the SMEs. Adopting the stratified random sampling technique, 10 enterprises covering all categories of the SMEs, which happen to be 5 per cent of the total of 198 units, have been chosen for the study. Ten years from 1999-00 to 2008-09 are chosen as the study period.

The data is collected from both primary and secondary sources. The sample enterprises and their entrepreneurs; financial data regarding the facilities provided and measures taken for the SME sector from various institutions and departments engaged in the area of SME development such as Bulk Drug Manufacturing Association (BDMA), the Commissionerate of Small Scale Industries and District Industries Centres (DIC); and published reports of the Ministry of Micro, Small and Medium Enterprises (MSME) and also of the Commissionerate of Industries and from relevant books, reputed journals and newspapers reports.

Primary data both qualitative and quantitative is collected from a comprehensive pre-tested schedule of 50 questions administering to the entrepreneurs of the sample enterprises. The questions cover such aspects as socio-economic profile of the sample entrepreneurs, their aims and ambitions, motivating factors, facilitating factors of entrepreneurship, financial and promotional measures of the MSME etc.

Tools of Analysis

Both the primary and secondary data is processed through a computer and scientifically analysed. Appropriate mathematical expressions such as growth rates, percentages, averages, and statistical tools like Mean, Standard deviation, Coefficient of variance, Analysis of Variance (ANOVA), Sum of Squares, Degrees of Freedom, F-value, P-value etc., are used. Further appropriate techniques are also used wherever necessary in order to draw logical conclusions and to interpret the data meaningfully.
**Significance of the present study**

The development of SME is an index of the industrial development and the overall economic development of a developing country like India. The success of the economy mainly depends on the entrepreneurial skills and quality, competencies and performance of the people in general and those involved in the task of rapid industrialization. India has to find, nourish and develop competent SMEs. The present study of the different aspects of the SMEs in the Pharmaceutical industry of Andhra Pradesh is, therefore, relevant and significance.

**Chapter scheme**

The thesis organized in Seven Chapters.


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Chapter -VII: Summary of Findings and Suggestions – This chapter summarizes the arguments developed in the previous chapters, draws certain findings and also suggests some practicable suggestions for developing the Pharmaceutical Small and Medium Enterprises (SMEs) in Andhra Pradesh.

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