Chapter 4

Causes of Industrial Sickness

4.1 Introduction

After a detailed literature review done in Chapter 2, we identified certain causes of industrial sickness. These are also studied in terms of the definitions and practised concepts of industrial health as discussed in Chapter 3. Here, we provide a critical analysis of the causes related to industrial sickness in general which is essential for the subsequent part of the work carried out with focus on certain identified units of Kamrup district of Assam.

The causes of sickness of different types of industrial units are not always similar. Different industries may become sick under different circumstances. The causes, therefore, differ from industry to industry and even among units in the same industry. Numerous factors acting simultaneously push a unit in the track of sickness. The causes can be broadly divided into two categories-(1) Internal and (2) External. Internal causes are those which originate within the operational framework of the unit. They generally arise due to internal disorders in the major functional areas (viz., production, finance, marketing, personnel etc.) of an enterprise. These factors are within the control of the industrial unit and therefore may be termed as controllable factors. On the contrary, external causes include those whose origins are outside the operational framework of the unit. The causes are the outcome of the various changes in the social, economic, political and international environment.
faced by the industry. The industry has no direct control over these factors and therefore, these factors are described as uncontrollable factors of industrial sickness. However, “it may be stated that all the causes are inter-connected and remedial action for one cause may not bring any overall relief to sickness” [1].

4.2 Internal Causes of Sickness

The major internal factors responsible for the widespread sickness in Indian industries are discussed below:

1. **Financial Bottlenecks**- An industrial unit if not managed properly makes severe mistakes in the area of finance thereby aggravating the problem of internal cash generation. This will, in turn, lead to deterioration in the liquidity position of the unit. There are various financial factors responsible for financial mis-management and consequent sickness in the industrial units.

   (a) **Lack of Financial Planning/ Control and Budgeting**- Financial planning/ control and budgeting are indispensable for an industrial unit to meet its day to day financial obligations. Absence of these measures adversely affects the reputation of a unit and ultimately leads to sickness.

   (b) **Improper Utilization of Assets**- The health of an industrial unit depends on the proper utilization of assets held by it. Improper utilization implies that the concern is not achieving the maximum turnover with its existing assets. This leads to unused installed capacity and eventually to sickness of the unit.

   (c) **Inefficient Working Capital Management**- The effective management of working capital portfolio by a unit determines its smooth functioning. Working capital management includes inventory and receivable management and liquidity management. A company fails to manage its working capital portfolio efficiently faces difficulties in meeting its day-to-day requirements and in raising additional funds for immediate needs.
(d) **Improper Diversion/ Siphoning off Funds**- A financially sound company meets its long-term requirements by raising long-term loans and short-term requirements are met through short-term loans. When this financial mix (short and long-term) is not optimum, the unit may have to divert long-term funds to short-term uses and vice-versa. This would disturb economic viability of the company and may lead to sickness [3]. Again sometimes the managements may siphon off its funds from the enterprize to serve their own ends. “This can be done by making purchases from associate concerns at prices higher than the prevailing ones, selling goods at lower prices; entering into contract with sole selling agencies and allowing handsome commission or discount on such sales etc. Even if an entrepreneur does not have an associate concern, he can do the same by dubious means.” [4].

(e) **High Rate of Capital Gearing**- A mis-managed company with high capital gearing is more prone to sickness. The term ‘capital gearing’ implies the volume of long-term fixed interest bearing securities as a percentage of total capital employed. The funds of a company can be raised from different sources which consist several types of long-term debts including bonds, debentures and preference shares. The rate of interest of long-term debts is fixed irrespective of profits. But equity dividends depend entirely on the profits of the company. Loans are, therefore, preferred to equity when a company goes into bankruptcy. But the use of loans carrying fixed rate of interest is beneficial till the capital gearing/financial leverage is favourable. If a company earns more on its total capital employed than the fixed rate of interest on loans or vice versa, capital gearing is said to be favourable. Thus the use of long-term fixed interest bearing loans beyond a certain level or limit pushes the company into liquidity crisis. This will, in turn, compel the company to borrow
still more from the banks and financial institutions and consequently aggravate its problem of high gearing [5].

In India, bank credit and loans from term-lending institutions constitute about 75 to 90 % of the total capital employed in the majority of small scale industrial units [6].

(f) **Poor Collection of Bad and Doubtful Debts** - Recovery of bad and doubtful debts is a long and arduous process. When such debts become substantial, it will wipe out a part of the capital and reserves of the enterprise and may lead to failure.

(g) **Lack of Ploughing Back of Profit** - Ploughing back of profits is a very economical source of finance. It helps an industrial unit to fight against depression and seasonal fluctuations. But failure to pay heed to this source by the entrepreneurs leads to financial crisis in the wake of economic depression or demand recession [7].

2. **Production Problems** - The various problems arising out of malfunctioning in the production function in an industrial unit are discussed below:

(a) **Improper Selection of Site** - Improper selection of site is one of the important contributing factors that may lead to failure of an industrial unit. Several factors should be taken into account in selecting the site of an industrial unit which in future determine its healthy functioning. The availability of infrastructural facilities like power, transport etc., the nearness of the sources of raw materials and the markets of finished goods, the availability of skilled labour etc. are some of the relevant considerations needed for setting up of industrial units. Improper selection of site, therefore, adversely affects the functioning of a unit and can cause sickness. Some sugar units of different states in India are appropriate examples of inappropriate choice of site.

(b) **Poor Maintenance of Plant and Machinery** - Proper maintenance of
plant and machinery is necessary for keeping machinery free from malfunctioning and excessive wear. Inadequate maintenance leads to frequent break down of machinery and thus disrupts the entire production programme. A World Bank Team pointed out that the maintenance programme of Indian Textile Mills were very poor and far below the West-European standard.

(c) **Inappropriate Plant and Machinery**—Inappropriate plant and machinery can also cause sickness to an industry. If the plant and equipment are uneconomical, obsolete and inefficient, both the quality and quantity of output of the unit will decline and cost will go up. Absence of modernization, i.e., the new techniques and methods of manufacture will also bring down the productivity of the unit and raise the cost. All these ultimately lead to failure of the industrial units. Lack of modernization has been the crucial problem of the cotton textiles and jute manufacturing industries in India.

(d) **Faulty Production Programme**—Production planning helps an industrial unit in getting available resources at every stage of production and thus ensures full utilization of plant, equipment and labour. In a faulty production programme, the unit has to stop its productive operations because of the non-availability of essential materials and components at the right time. As a result, the plant and labour have to remain idle at various stages on one hand while the accumulation of material increases on the other.

(e) **Lack of Product Diversification**—The growth of an industrial enterprise depends to a great extent on diversification of products. Lack of product diversification pushes an enterprise in the tract of sickness. An enterprise relying on a single product encounters various problems such as competition, scarcity of raw materials, decline in demand, rise in prices of raw materials etc. “In India examples of diesel oil engine and kerosene
lamp industries are standing examples of failure of units due to lack of product diversification” [8].

3. **Marketing Constraints** - The important internal causes of sickness due to internal aberration of this functional area are as follows:

   (a) **Inept Demand Forecasting** - The quantity of production of an industrial unit is determined by making an estimate of the future demand. An inept forecasting of demand can cause various problems to an industry. If the unit overestimates its future demand, it may turn sick as the product produced will not find a ready market.

   (b) **Selection of Inappropriate Product-Mix** - An inappropriate product-mix may cause sickness to an industry. An industrial unit can produce different products with various combinations of same resources. For example, a steel furniture manufacturing unit can make chairs, tables, cupboards, book racks, almirahs etc. using same equipment and labour. The profit of the unit depends upon the sales of the quantities of different products, i.e. the product-mix. The enterprize would be suffering even if its production and sales are increasing if the sales of profitable items are declining and those products where margin of profit is inadequate are increasing.

   (c) **Lack of Market Research / Survey** - Market research plays an important role for getting ideas about customers’ habits, desires, needs and acceptability of different products. Research, thus, helps an industrial unit in framing an effective and strong marketing policy. Lack of proper research fails to meet the consumers’ wishes in this fast changing world and may, therefore, cause failure to industrial enterprizes.

   (d) **Absence of Proper Product Planning** - Proper product planning is essential for an enterprize in order to maximize its profitability. Sometimes certain old products of an enterprize may become obsolete or inap-
propriate in the long run. Therefore, proper planning for the development and marketing of new products is indispensable if the firm wants to maximize profit. Absence of such planning may lead to sickness.

(e) **Reliance on a Few Customers** - The industries which place too much reliance on the demand indicated by a few customers are always prone to sickness. The reason is that if the customers change their demand or the product becomes obsolete, the industries would be in dire financial crisis.

(f) **Inappropriate Sales Promotion** - An appropriate sales promotion policy is essential for the smooth functioning of an industrial unit. There are various factors on which the sales promotion of a particular product of an enterprise depends, such as, its nature, usage, market segment, the habits of the customers etc. Failure to formulate an appropriate sales promotion policy disrupts the functioning of the unit and may cause sickness.

4. **Problems of Personnel** - The internal causes of sickness because of malfunctioning of this system are as follows:

(a) **High Absenteeism and Labour Turnover** - High absenteeism and labour turnover which are common features of many industrial units may cause sickness. The machines and equipments would remain idle and uninterrupted working of the units would be disturbed.

(b) **Bad Industrial Relations** - Harmonious relationship between labour and management is very essential for the health of an industrial unit. Poor labour-management relations and labour disputes cause low productivity, poor quality of products, inadequate maintenance of plant and machinery, increase in wastage and often lead to demonstrations, strikes, lock-outs etc. Gheraos, lock-outs, strikes etc. result in loss in man-days and thus reduces the production of the industries. If such situation prevails for longer period, it will lead the units to sickness.

(c) **Inappropriate Wage and Salary Administration** - An industrial unit
paying wages and salaries lower/higher than the prevalent wages in the industry in general, it faces some serious problems. If it pays less it would lose experienced employees and consequently suffers from decline in productivity. Similarly, payment of high wages raises the cost of production. Inappropriate wage and salary administration, therefore, causes sickness.

(d) **Overstaffing**- Different skilled and trained persons are generally needed for operating different machines and equipments in an industrial unit. Sometimes in some enterprizes it is observed that there are more men than jobs available to them. The reason is that persons with appropriate skill and training are not recruited in the unit and the scarcity of such persons is made up by recruiting more unskilled and untrained persons. Absence of manpower planning is the most important cause of such problem. Overstaffing not only hampers production but also leads to wastage in money paid to the excess staff of the unit. In such situations, the enterprizes face financial crisis and hence fall sick.

5. **Corporate Management**- The prime cause of sickness of an industrial enterprize is the poor management. “Poor management is that management which lacks requisite personnel, expertise skills and adequate information and reporting systems at the top” [9]. The studies conducted by different financial institutions and committees concluded that managerial incompetence was the predominant cause of business failure.

A Study Team of the State Bank of India in its report highlighted the fact that there was no planned approach to the activities in the key functional areas, such as, finance, marketing and production. The Team further stated that there was lack of financial discipline particularly in the management of working capital and no effort was made to build up internal financial strength [10]. The study conducted by the Reserve Bank of India revealed managerial deficiency and out-right management as the single largest cause of industrial sickness in the large scale sector. Tiwari Committee Report, 1984 further
highlighted that overwhelming causes of business failure were management

Deficiency in management may arise because of the following:

(a) **Poor Managerial Talent**- Managers in industrial enterprizes should possess certain traits such as maturity, decisiveness, intelligence, supervisory ability etc. Absence of managerial talent creates disorder in all fronts of operation of the enterprize. The managers with poor talent are unable to solve the various problems faced by the enterprizes during different periods leading to failure of such enterprizes. “Worse still is the fact that there is a tendency to take into employment numerous relatives and friends, who by their training and performance are not capable of performing functions entrusted to them” [12].

(b) **Poor Reporting**- Lack of proper information and reporting system particularly accounting information is another important cause of industrial sickness. Various deficiencies have been noticed relating to the information and reporting system that contribute to sickness. The important deficiencies are: (a) no or poor budgeting control, (b) no or poor costing system to calculate effective cost of each product, (c) no or poor cash flow planning and (d) poor reporting of faults, breakdowns and sales in the industry. The lack of adequate information and reporting system makes impossible for the management to analyze the growing problems and to take appropriate steps for its early solution.

(c) **Mismanagement**- In many cases, management of an enterprize deliberately indulges in mismanaging the affairs for its own advantages. This wilful mismanagement and dishonesty may drain away the profits of the enterprize and may lead to business failure.

(d) **Infighting**- Infighting among the different groups of management, i.e., partners of a firm or directors of a company has been one of the important causes of industrial sickness. On account of these dissensions most of the
resources go waste, there is general air of financial stringency. In such a situation, the enterprise is compelled to face serious consequences and hence falls sick.

(e) Inability to Respond- Another important internal factor responsible for sickness is the failure of management to respond adequately to changes. In present day economic world an industrial unit cannot operate in isolation. It has to act upon and react to a continually changing environment. Some of these changes take place slowly and thus predictable in nature, while other occurs suddenly and cannot be predicted. If the firm fails to foresee such invents in time and estimates their impact, it would eventually face a crisis. The changes may relate to competitive, political, economic, social and technological changes taking place [13].

(f) Improper Project Planning- Project planning is essential for healthy functioning of an industrial unit. But in many cases, due to lack of managerial ability and expertise, project planning is not done properly. Many projects are born sick. This may be because of improper forecasting of demand for the products, faulty choice of technology, improper forecasting of financial requirements etc. As a result the various stages in project progress are not reached as per schedule and get delayed. For example, there might be delay in the completion of the building, the plant and equipment did not arrive in time or the installation could not take place as projected. This is further aggravated by delay in the supply of further instalment of loans from the financial institutions contributing to further time and cost overshoots in project. “Poor implementation is a general feature in Indian environment because of the shortage economy which sometimes is real and quite often manipulated. The management of project has to be aware of the key materials needed for the project, the lack of which can delay the project progress. Contingency planning has, therefore, to be thought of to overcome such situations when they
arise and are anticipated [14].

4.3 External Causes of Sickness

The major external causes of sickness are discussed below:

1. Financial bottlenecks- The various causes of sickness under this category are as follows:

   (a) **Lack of Adequate Industrial Credit**- Both short and long-term finance are essential for an industrial unit for its smooth operation. Non-availability of adequate finance may create vital operational problems and cause sickness.

   (b) **Delay in Disbursement of Loans**- Delay in disbursement of loans by banks and financial institutions has been one of the important causes retarding industrial development in certain sectors. Particularly, the small scale industries suffer from the problem of delayed availability of bank finance and consequently fall sick.

   (c) **Unfavourable Investment Climate**- When the investment climate in the country is not favourable, a unit will not be able to raise funds by floating shares and debentures in the market as people may not like to invest in the companies in such a period [15].

   (d) **Policy of Credit Restraints**- Policy of credit restraint followed by credit institutions at a time when the industrial units are in urgent need of funds may cause sickness.

2. Production Problems- Production problems arise due to the following reasons:

   (a) **Shortage of Inputs**- Scarcity of inputs can affect the health of the industrial enterprises. If an industrial unit is unable to obtain the essential
inputs like power, fuel, raw materials etc., it reduces the capacity utilization and may be a major reason for hold up of its production. When this situation continues for a long time, the unit may turn sick. Non-availability of inputs, particularly power has been a major factor hampering the progress of many Indian industries. The Eastern and North-Eastern regions of our country have been suffering from the scarcity of power since a long time.

Scarcity of raw materials can also cause serious set-back to some industrial concerns. The Mini Steel Plant Industry is a case in point. The impact of scrap shortage on the Electric Arc Furnace (EAF) units has been drastic. A survey conducted by the Steel Furnace Association of India (SFAI) in December, 1991 among 40 units showed that 10 units had become sick, 17 furnaces had been closed down and 30 were working below 60% capacity [16].

(b) Restrictions on Imports- The government at times imposes heavy restrictions on the import of some materials and machineries. As a result, most of the units specially engineering and electric goods producing units encounter the problems of shortage of materials and equipments which ultimately lead these units to sickness.

3. Marketing Problems- The causes of sickness due to malfunctioning of this system are as follows:

(a) Demand Recession-Demand recession leads to a decline in sales of the enterprise. It hampers the efficient operation as huge unsold stock piles up continuously. When this recession continues for longer period, it results in under utilization of the installed capacity of the concern and may lead to a situation of prolonged ailment.

(b) Heavy Taxes-Introduction of excessive taxation policy especially in respect of excise and import duty by the government continues in increasing
the cost of production. This further results in a hike in the prices of the products and consequently the firms face a problem of contraction in demand of the products.

(c) **Curtailment of the Purchases by Bulk Purchasers**- Some industries sell a major chunk of their goods to certain government departments. Curtailment of purchases by these departments for some reasons creates crisis and causes sickness. Again delay in the payment of government purchase may also land the industry into financial stringency. Besides these, liberal licensing of the industrial enterprises, inability to keep pace with the changes in the international market etc. are some of the causes of sickness under this category.

4. **Personnel Problems**- The causes under this category are:

(a) **Non-availability of Skilled Manpower**- Industries located in the backward areas suffer from the scarcity of skilled manpower though there is abundant supply of unskilled labour. Lack of availability of skilled labour not only reduces production but also retards the overall progress of the industries.

(b) **Labour Unrest**- Labour unrest such as, strikes, lock-outs, etc. leads to low productivity or less utilisation of available resources, loss of man-hours and consequently decline in profitability of the industrial units. In a study conducted by the RBI for 341 sick industrial units, 22.3 % was affected by labour trouble or poor labour relations [17].

(c) **Wage Disparity in Identical Units**- An efficiently managed and organized unit can offer better salaries and other facilities than mismanaged units. A skilled worker always prefers to shift to an employer who can offer better remuneration and facilities. In such a situation, an inefficient unit faces difficulties in retaining skilled and efficient workers. Scarcity of experienced and skilled employees may lead to a unit to destruction.
(d) **Inter-union Rivalry**- If there are multiple unions within an industrial unit, inter-union rivalry may also sickness.

### 4.4 Conclusion

Here, we have discussed the primary causes of industrial sickness. There are two broad classes of causes related to industrial sickness. These are internal and external. All of these causes should be properly identified to study the industrial sickness phenomenon in this entirety. We here have discussed these causes with as much as details possible which shall lay the foundation of the work included in the subsequent chapters.
References


