CHAPTER-VIII

SUMMARY, CONCLUSIONS AND SUGGESTIONS
SUMMARY

I. INTRODUCTION

Small-scale industries play an important role in the economies of the developed and developing countries as they enlarge employment opportunities, secure dispersal of industries and lead to the broad-basing of entrepreneurship. Realizing the strategic role of these industries in the industrialization of the country the Government of India and the State Governments have all along been following the policy of encouragement, protection and promotion of such industries. This has resulted in a commendable quantitative and qualitative growth of the small-scale industrial sector in India.

But the small-scale industries in India face a number of financial, marketing, managerial and technical problems and suffer from inadequate supply of many critical raw-materials and lack of proper sub-contracting machinery. Most of small industrial units have old and outdated machinery and equipment which they are unable to replace with the new and modern equipment and machinery due to their own meagre financial resources and non-availability of adequate financial assistance from the multiple institutions which exist in the country to support them.

Till now public attention in this country has been focussed so much on the performance of large-scale industries and that the dismal performance of innumerable units promoted and managed by small entrepreneurs is going almost unnoticed. Several studies, seminars, symposia and meetings have been conducted on the rationale, growth and working of public enterprises and large-scale private sector. Distinguished economists and experts also paid their attention only to the problems of large-scale industries. Of the several aspects of Small-scale Industries management, it is the finance function that remained a darker area with no attention paid so far. The history of small-scale industries is replete with instances of mismanagement and lack of financial discipline. Even to-day, many small industries continue to suffer from the legacy of financial indiscretions and indiscipline. It is a fact that a large number of Small-scale Industries have no manual which lays down the procedure for the compilation and maintenance of accounts and an effective internal Audit system. Similarly, many of the enterprises do not have sound capital budgeting procedures, some do not have systematic
cost records and inventory control methods. In many a case, the credit and collection systems are weak and large capital is blocked in inventories and receivables. It is in this context, an attempt has been made in the present study to analyse the problem of financial management of Small scale Industries with special reference to small-scale industries in Haryana.

Objectives of the Study

The main aim of the study is to identify the financial problems of the small-scale industries in Haryana and suggest some measures for effective financial management of these industries, so as to make them financially viable. The study specifically aims at the following:

(a) To evaluate the general planning, financial planning and profit planning including the tools of profit planning used by small firms;
(b) To examine the financial information system of small-scale industries;
(c) To study the management of different components of working capital, viz., cash, receivables, and inventory, in order to determine the degree of efficiency with which each of these components are managed;
(d) To examine the important factors considered by small units while taking financing decisions and planning of capital structure and use of capital structure theories;
(e) To examine whether capital budgeting technique is used or not for taking capital investment decisions and priority of the projects is fixed or not;
(f) To examine the various sources of financing in small-scale industries; and
(g) Finally to make appropriate suggestions for policy makers for the more effective financial management of the industries to make them financially viable.

Scope of the Study

The present study deals with the small-scale industries in Haryana. It was not possible to cover all the States in India due to time and financial constraints. However, it can be said that the findings of the study would have equal applicability for the enterprises in other States also, as there is much similarity among the small industries with respect to size, structure, operation and management.
There are certain industries which are outside the scope of the small industry sector. These industries are handicrafts, handlooms, power looms, Khadi and village industries, coir and silk industries. These industries come under the purview of the respective Boards or Commissions.

**Data Requirement**

The present study is based on both secondary and primary data. The secondary data have been collected from the Directorate of Industries, Chandigarh, Haryana and Office of the Small-scale Industries Development Commissioner, New Delhi.

The primary data have been collected through questionnaire, interviews and observations. Primary data are the main base of the study. For this purpose the researcher has undertaken intensive case studies of 400 selected small-scale industries in Haryana. Primary data have been collected from Financial Managers/Owners and Management of Small-scale Industries. The initial draft of the questionnaire have been tested through a pilot study of five units and the shortcomings found in the questionnaire have been removed.

**Size of the Sample**

According to the latest information available from the Directorate of Industries, Haryana, there are 83,448 registered small-scale industries in Haryana as on 31st Dec., 1999. As we could not make an indepth study of all the units registered in Haryana, we have selected 400 units from all over the State, which comes to 0.5 per cent (approx.) of the universe. While selecting these units enough care has been taken to see that these are representative of all types of industries situated in all districts of Haryana. For the said purpose we have divided all the industries into six categories such as Garments, Auto-parts, Electronics, Metal Products, Rubber & Plastics and Others.

II. PLANNING FUNCTION

**General Planning in Small-scale Industries**

Planning is decided in advance what will be done in both short and long-term. It must include the following process: (1) establishing the objectives of the firm, (2)
formulation strategies, (3) determining operating policies, and (4) creating procedures. In the dynamic small business, the planning function is given less consideration, yet it may be the most important function that the manager performs.

In small-scale industries just 39.3 per cent industries are properly making plans for the future. On the other hand 42.7 per cent units are making plans in unwritten form without determining operating policies and formulating strategies. This shows non-seriousness of small firms' managers towards important function of planning. Planning function is performed in small industries according to their size. In large units of small-scale sector planning is being done properly. Whereas in small units of small sector planning is in unwritten form or not done at all. In Auto-parts industry due to their large size, proper planning is made in 75 per cent units. But in Metal Products industry only 7.7 per cent units are making proper plans and 53.8 per cent units make plans without involving paper work. The reason for this is the small size of most of the units in this industry. In Garments industry 52.5 per cent, in Others industry 41.9 per cent, in Electronics industry 41.6 per cent and in Rubber and Plastics industry 32.1 per cent are making plans in writing. In small-scale industries 18 per cent industries are not planning. Most of these are the very small sized units managed by sole proprietor. In this category the maximum percentage is of Metal Products industry, 38.5 per cent followed by Others industry 22.1 per cent, Rubber and Plastics industry 21.5 per cent, Electronics industry 11.7 per cent, and Garments industry 5 per cent.

In small firms planning function is performed mainly by owner(s)/management without taking the help of experts. Only in larger units help of experts is taken while making plans for the future. That is why only in 10 percent Auto-parts industries followed by 5 per cent Garments industries, 4 per cent Rubber & Plastics and Others industries, 3 per cent Electronic industries, and just 2 per cent Metal Products industries are making plans with the help of experts.

Organisation chart is also prepared by largest units of small sector particularly private limited or Public Ltd. Companies. In Auto-parts industry 5 per cent followed by in Garments and Others industries 4 per cent, in Electronics industry 3 per cent and in Rubber and Plastics industry 2 per cent are maintaining organisation chart.
In small-scale industries monthly planning is more popular. 54 per cent industries make plans for a month. Six months planning is done by 31.7 per cent industries. And yearly planning is done by just 14.3 per cent industries. The period of plans mainly depends on the nature of work and size of the units. In Metal Products industry most of small units do job work and that is why 72.9 per cent are doing monthly planning. In remaining industries approx. 50 to 60 per cent are doing monthly planning except in Garments industry where only 35.5 per cent units are making monthly plans. In Garments and Others industries six months planning is more popular and 40 per cent units in these industries are making plans for six months. Whereas in Auto-parts, Electronics, Metal Products and Rubber & Plastics industries just 20 to 28 per cent units are making plans for a period of six months. Yearly planning is done maximum in Garments industry by 25 per cent units and the percentage is minimum 6.3 in Metal Products industry. In remaining industries 10 to 15 per cent are making yearly plans.

As far as fixation of standards are concerned in Garments and Auto-parts industries 95 per cent are using this technique. Whereas in Electronics industry 90 per cent are fixing standards for comparison and in remaining 80 to 85 per cent are fixing standards.

Financial Planning in Small-scale Industries

Financial planning is the process of determining the objectives, policies and procedures relating to the financial activities of an organisation. It involves the preparation of plans for the procurement, investment, administration of funds.

In small-scale industries, answer to the question “Do you make financial Plan?” was in ‘yes’ by 80 per cent units. And on the basis of this answer we can say that in Auto-parts industry maximum 93 per cent units are doing financial planning followed by Electronic industry 90 per cent, Garments Industry 89 per cent, Others industry 75 per cent, Rubber and Plastics industry 72 per cent. Minimum 67 per cent in Metal Products industry are making financial plans. But in the observation of the researcher financial planning in real sense is worked out by much less units. Because most of small firms’ owners/managers do not know the meaning of financial planning properly. To them, financial planning means arranging finance. This fact is substantiated by the answer of
the question “Who makes financial plan?” In just 15 per cent industries the services of experts are taken for making financial plans and in rest of the industries the owners/management themselves make financial plans.

In small-scale industries 85.1 per cent industries are spending less than a week on planning function in a year. And just 1.5 per cent industries are spending 15 to 30 days on planning in a year. Rest 13.4 per cent industries are spending more than a week but less than 15 days on planning. Time spent on planning depends on the length of the plan period.

**Profit Planning in Small-scale Industries**

In simple terms profit planning means forecasting the long-term future earnings of the company. So, the profit plan is basically an indication on the part of the firm’s owners as to their profit goals.

In small-scale industries 61 per cent units are making profit plans. In Auto-parts industry, this percentage is maximum, 7.5 per cent, whereas in Metal Products industry this is minimum 38.5 per cent. The main reason for this is, the small size of units in Metal Products industry where units cannot hire the services of experts for making profit plans. In Electronics industry 66.7 per cent, in Others industry 65.1 per cent, in Garments industry 65 per cent and in Rubber & Plastics industry 64.3 per cent units are making profit plans.

**Use of Break-Even Analysis Tool in Profit Planning in Small-scale Industries**

Break-even analysis represents an important tool in profit planning. The relationship among cost of production, volume of production, the profit and the sales value is established by break-even analysis.

In small-scale industries profits are estimated in 81.2 per cent industries without using the important tool of profit planning. It means the small industries are estimating profits of the future without establishing relationship among cost of production, volume of production, the profit and the sales value just on the basis of past experience. Only 18.8 per cent industries are using Break-even Analysis tool in profits planning. The main
reason for this is that it requires services of experts which the small units cannot afford. In Auto-parts industry maximum 26.7 per cent units followed by Others industry 21.4 per cent, Electronics industry 17.5 per cent, Garments industry 17.3 per cent, Rubber and Plastics industry 16.7 per cent, and in Metal Products industry 13.3 per cent units are using this important tool in profit planning.

Sales Forecasting in Small-scale Industries

In small-scale industries 67.7 per cent of the total industries under study forecast sales for the future. The maximum percentage is 75 in Auto-parts industry followed by Electronics industry 70 per cent, Rubber & Plastics industry 67.9 per cent, Garments Industry 67.5 per cent, Others industry 66.3 per cent and in Metal Products industry 64.1 per cent units which forecast sales. In other words we can say that on average one unit out three units in the small sector is not forecasting future sales.

Use of Sales Forecast Techniques in Small-scale Industries

The various approaches of forecasting sales can be divided into three categories: the Judgment-based method, Quantitative models, and Other methods.

In small scale sector judgment based method is most popular. 93.7 per cent units of the total 67.7 per cent industries which are forecasting sales are using judgment based method. In this method on the basis of past experience by keeping in mind the expected changes, sales forecast is prepared. Quantitative Models, being a mathematical technique, is used just by 2.2 per cent units in the small sector. These are used only by large and modern units which can afford the services of experts. These are used only by 7.4 per cent units in Garments industry and 3.5 per cent units in Others industry. Other methods of forecasting sales are also not much popular in small firms. Only 4.1 per cent are using Other methods for sales forecasting. In this category maximum percentage is 12 per cent in Metal Products industry. In Rubber & Plastics and Others industries just 5.3 per cent are using Other methods for sales forecasting.

Expenses Forecast in a Small-scale Industries

For profit planning the two key elements are sales and related costs and expenses.
In small-scale industries under study only 60 per cent are forecasting expenses. In Auto-parts industry the percentage of units forecasting expenses is maximum 70 per cent, followed by Electronics industry 66 per cent, Others industry 64 per cent, Garments industry 62 per cent and in Rubber and Plastics industry 60 per cent. In Metal Products industry the minimum percentage that is just 38 out of hundred units are forecasting expenses.

III. INFORMATION SYSTEM

Proper Accounting System in Small-scale Industries

In day-to-day life the management has to take several decisions in any business concern. The soundness of financial decisions taken by management depend upon the accessibility of accurate, meaningful, and timely financial information. The financial information of any firm comes from its accounting system.

In small-scale industries proper books of accounts are maintained by 92 per cent industries. Only very small units are not maintaining proper accounts. In the Auto-parts industry 97.5 per cent units are keeping account of their transactions properly. Whereas in Metal Products industry as majority of units are comparatively of small size, 85.9 per cent units are properly preparing books of accounts. In Garments industry also, small units such as Tailoring Houses are not maintaining books of accounts (10% units). In remaining industries 5 to 6 per cent units are not maintaining accounts.

In small sector for the purpose of maintenance of accounts, majority of the industries appoint one or two persons either for full time or part-time. Only in 6.5 per cent industries mainly in large units of the sector working under the organisation of company (as a Private Ltd. or Public Ltd. Company) separate department for accounts has been established. In Metal Products industry just 3 per cent units are having separate accounts department. Otherwise 5.9 to 8.6 per cent units in the remaining industries are having a separate accounts department. It means in small-scale industries more than 90 per cent industries are maintaining accounts books by appointing one or two persons for full time or part-time.
Use of Cost Reduction Techniques in Small-scale Industries

Due to comparatively more competition in small-scale industries, it becomes necessary to use some techniques of cost control in small firms for survival. But we see that only 10 per cent big units of small sector are using cost reduction techniques. The maximum percentage is in Auto-parts industry that is 20 per cent units, which are using cost reduction techniques. The reason for using cost reduction techniques by maximum number of units in Auto-parts industry is the intense competition. In Others industry 16.3 per cent units are using cost reduction techniques followed by Electronics industry 8.3 per cent, Rubber & Plastics industry 7.1 per cent, Garments industry 5 per cent and least in Metal Products industry just 3.8 per cent units are using cost reduction techniques.

Funds Flow and Cash Flow Statements in Small-scale Industries

To analyse the main sources and applications of funds and cash generated as well as used during the accounting year in small scale industries, the preparation of the two important statements i.e. Funds Flow Statement and Cash Flow Statement is not very popular. Only 29.3 per cent industries in the small-scale sector are preparing both or one of these statements. And most of these industries are working as a company or partnership firm. In Auto-parts industry 70 per cent industries are preparing these statements followed by Others industry 34.9 per cent, Garments industry 33.7 per cent, Electronics Industry 18.3 per cent, Rubber & Plastics industry 17.8 per cent. In Metal Products industry just 15 per cent units are preparing these statements.

Amount spend on Maintenance of Accounts in Small-scale Industries

It is true that today, even in small-scale industries 90 per cent units are maintaining proper Accounts of their transactions. But when we analyse that how much amount of their sales in percentage is spent on maintaining accounts, we see that just only 10.3 per cent units are spending more than 1 per cent of their sales annually on maintenance of accounts. So, it is clear that even today, in small-scale industries 90 per cent (approx.) are spending even less than 1 per cent of sales on accounting. In Electronics, Auto-parts, Others and Garments industries 11.3 to 13.3 per cent units are spending more than 1 per cent of their sales on accounting. These are mainly biggest
units in the small sector. In Metal Products and Rubber & Plastics industries 6.4 per cent and 7.2 per cent units respectively are spending more than 1 per cent of sales on accounts. In small-scale industries majority of industries (61.5%) are spending 0.6 to 1 per cent of their sales on accounting. And 20.2 per cent industries are spending 0.1 to 0.5 per cent of their sales on maintaining proper accounts. The main conclusion is as the size of units increased the percentage of amount spent on accounting increased. Very small units (8%) are not spending any amount on accounting.

**Income and Expenses Budget prepared by Small-scale Industries**

A budget is a detailed plan of operations for some specific future period. It is an estimate prepared in advance of period to which it applies.

In small-scale industries only 20 per cent industries are preparing income and expenses budget for watching incomes and expenses. In Auto-parts and Electronics industries 33 per cent units are preparing income and expenses budget followed by in Others industry 26 per cent units. In Garments industry 15 per cent units, in Rubber & Plastics industry 12.5 per cent and in Metal Products industry just 7.6 per cent units are preparing income and expenses budget.

**Internal Control System in Small-scale Industries**

Internal control system is important in safeguarding the firm’s assets and also plays a key role in enhancing the quality of the financial output employed in the decision-making process. Internal control has long been recognised as important in the large companies. But, in small-scale industries maintaining internal control is difficult. The absence of diverse staff makes the division of responsibility impractical at times. That is the reason that only 7 per cent units in small-scale industries under study apply a properly developed system of internal control. In Auto-parts industry 10 per cent units followed by Electronics industry 8 per cent, Garments industry 7.5 per cent, Others industry 7.4 per cent, Rubber & Plastics industry 6 per cent and the Metal Products industry 4 per cent units are using internal control system. The units which are using internal control system are big units which can afford the services of experts.
Comparative Statements in Small-Scale Industries

For the purpose of inter-firm and inter-period comparison, comparative statements can be prepared. These statements indicate trends in sales, cost of production, profits etc., helping the analyst to evaluate the performance, efficiency and financial condition of the firm.

In small-scale industries only 30 per cent industries are preparing comparative statements. Most of them are preparing for the purpose of inter-period comparison. In Auto-parts industry 45 per cent units are preparing comparative statements whereas in Metal Products industry only 15 per cent units are doing the same. In Electronics industry 33 per cent, in Garments, Others and Rubber and Plastics industries 27 per cent, 26 per cent and 24 per cent units respectively are preparing comparative statements. Again, this exercise is undertaken only by comparatively big units.

Cost Accounts in Small-scale Industries

Cost accounting has become an absolute necessity for functioning in the large multi-divisional firms operating in different localities. But, it does not mean that cost procedures are not important in small enterprises.

In small-scale industries, even today, cost accounting is considered useless. That is why only 4 per cent units are maintaining cost accounts. In Auto-parts industry 7.5 per cent, Electronics industry 5 per cent, Garments industry 3.7 per cent, Rubber & Plastics 3.6 per cent in Others industry 3.5 per cent, and in Metal Products industry just 2.5 per cent units are maintaining cost accounts.

Pricing Policy of Small-scale Industries

There are numerous factors which affect the pricing policies and decisions of a firm.

In small-scale industries the main base of price fixation is competition. In 64.8 per cent small industries prices of their products are fixed by keeping in mind the competition. In Garments industry 81.2 per cent units are using competition-oriented pricing policy. The main reason for this is that the product cannot be differentiated easily.
by everyone. In Auto-parts industry 70 per cent units followed by Electronics industry 63.3 per cent, Metal Products 61.5 per cent, Rubber & Plastics industry 60.7 per cent, and in Others industry 53.5 per cent units are fixing their prices on the basis of competition.

On the other hand, in 23.5 per cent industries prices of the products are fixed on the basis of cost of the product. This method is adopted mainly by those units who want to play safe. The maximum percentage is 34.9 in the Others industry category which are using cost-oriented pricing policy closely followed by Rubber & Plastics industry with 34 per cent units, Electronics industry 23.3 per cent, Metal Products industry 20.5 per cent and least by Garments industry where 8.8 per cent units which are determining prices of their products on cost basis.

Remaining 11.7 per cent small-scale industries are using other methods of price fixation. In this category the maximum percentage is of Metal Product industry 18 per cent. These 18 per cent units in Metal Products industry charge prices according to the design, quality and time period for executing the order. In Garments industry 10 per cent units and in Electronics industry 13.4 per cent are determining the prices of their products under value based pricing method. In the same way 10 per cent units in Auto-parts industry, 11.6 per cent units in Others industry, and 5.3 per cent units in Rubber & Plastics industry are using other methods of price fixation.

IV. WORKING CAPITAL MANAGEMENT

Working Capital Management in Small-scale Industries

Working capital management is an integral part of overall corporate management. To a financial manager, a working capital sphere throws a welcome challenge and opportunity. In view of the multiplicity of factors exerting varied degrees of influence of working capital studies, a management has to be alert to the internal, external and environmental developments, and constantly plan and review its working needs and strategy.

Out of total small-scale industries in Haryana, 57.3 are planning working capital well in advance. In Auto-parts industry 82.5 per cent units are properly planning working capital requirements and its arrangement well in advance followed by Garments industry
In small-scale industries on the other hand 42.7 per cent industries do not plan working capital. In this category most of units are smaller one. These small units have some sort of limited facility provided by banks for working capital requirements. In this category maximum percentage is of Metal Products industry 60.3 per cent followed by Rubber & Plastics industry 46.4 per cent, Other industry 44.2 per cent, Electronics industry 40 per cent, Garments industry 36.3 per cent. In Auto-parts industry only 17.5 per cent units are not managing working capital properly.

Sources of Working Capital Financing in Small-scale Industries

Commercial banks play a most significant role in providing working capital finance.

In small-scale industries 84.7 per cent industries depend on commercial banks for their working capital requirements. In Garments industry 93.7 per cent units followed by Rubber & Plastics industry 89.3 per cent, Others industry 86.1 per cent, Electronics industry 83.3 per cent, Metal Products industry 76.9 per cent, and in Auto-parts industry 75 per cent units are getting their working capital mainly from commercial banks.

On the other hand small units in the small-scale sector or financially sound units are arranging working capital on their own or with the help of friends/relatives or by getting advance from customers. In this category there are 15.3 per cent industries which are fulfilling their working capital needs mainly from other sources. In the Auto-parts industry 25 per cent units followed by Metal Products industry 23.1 per cent, Electronics industry 16.7 per cent, Others industry 13.9 per cent, Rubber and plastics industry 10.7 per cent and in Garments industry just 6.3 per cent units are financing their working capital mainly from the sources other than commercial banks.

Cash Management in Small-scale Industries

Management of cash flows is one of the most important functions of the management of small firms. The control of cash is absolutely essential if a firm wishes to optimize its
efficiency. Cash budget is an important tool of efficient cash management. It serves both as a planning tool and a control device. But in small-scale industries only 38.2 per cent industries are using this tool for efficiently cash management. Out of these 38.2 per cent industries most of them are preparing cash budgets just to estimate the cash requirements and cash receipts. Only in bigger units cash budgets are also prepared for controlling the inflows and outflows of cash. Most of small units prepare cash budget only for a month or for a week. In Auto-parts industry 65 per cent units are preparing cash budget. In Others industry 43 per cent units followed by Garments Industry 40 per cent, Electronics industry 38 per cent, Rubber & Plastics industry 30.4 per cent, and in Metal Products industry just 23 per cent units are preparing cash budget for efficient cash management.

In small-scale sector 61.8 per cent industries are not preparing cash budget. In this category the leading industry is Metal Products with 76.9 per cent followed by Rubber & Plastics industry 69.6 per cent, Electronics industry 61.7 per cent Garments industry 60 per cent, Others industry 57 per cent. And least in Auto-parts industry 35 per cent units are not preparing cash budgets.

In small-scale industries there is no separate department exclusively for cash management. Cash matters are mainly looked after by the owner(s). In big units only a separate person is appointed for receipts and payments of cash. But all important decisions regarding cash matters are taken by the owner(s) in most of the small firms.

Various techniques of cash management can be used to control the cash inflows and outflows. In small firms only 18.3 per cent industries are using cash discount technique for speedy collection of cash. In Electronics industry maximum 23.3 per cent units are providing cash discount facility to its customers for early payments. In Garments industry 20 per cent, in Others industry 19.8 per cent, in Rubber and Plastics industry 17.9 per cent, in Metal Products industry 15.4 per cent, and in Auto-parts industry just 10 per cent units are providing this facility to their customers.

**Receivables Management in Small-scale Industries**

Receivable management is of utmost importance in small enterprises since receivables constitute approximately 25 per cent of total assets. Several policies directly
affect the size of receivables; (1) sales policies, (2) cash discounts, (3) length of credit terms, and (4) credit risks.

(i) Cash Discount Facility

As already explained in small firms cash discount technique is not very common. Only 18.3 per cent industries are using this technique to reduce their receivables. In the industry where credit period is longer, this facility is adopted for speedy collection of cash. In Electronics industry 23.3 per cent followed by Garments industry 20 per cent. Others industry 19.8 per cent, Rubber & Plastics industry 17.9 per cent, Metal Products industry 15.4 per cent, and in Auto-parts industry just 10 per cent units are providing discount for early cash payments to customers.

(ii) Period of Credit

In small-scale industries, the period of credit sales varies according to the value of the product. In small firms the maximum number of units (37.5%) are granting credit for an average period of 31 to 60 days closely followed by 36.7 per cent industries which are selling goods for an average credit period up to 30 days. Other 18.5 per cent industries are granting credit for 61 to 90 days and remaining 7.3 per cent industries granting credit for 91 to 120 days on an average. No one in the small sector is granting credit for more than 120 days.

In Metal Products industry maximum percentage of units (66.7%) are granting credit up to 30 days. In Auto-parts industry the maximum percentage of units (50%) are selling goods for average credit period of less than 31 days. In Electronics, Rubber & Plastics, Garments and in Others industries the maximum percentage of units (46.6%, 46.4%, 46.3% and 38.4% respectively) are granting credit for an average period of 31 to 60 days. In Others, Garments, Electronics, Auto-parts, Rubber & Plastics, and Metal products industries 32.5 per cent, 23.7 per cent, 16.7 per cent, 12.5 per cent, 10.3 per cent and 7.1 per cent units respectively are granting credit for the average period of 61 to 90 days. Only 7 to 9.3 per cent industries in small sector are offering 91 to 120 days as an average period of credit for selling goods.
Credit Evaluation

Before granting credit to a prospective customer the firm must evaluate the creditworthiness of the customer. There are several ways in which a firm can find out whether a customer is likely to pay its debts on time or not.

In small-scale sector, to measure the creditworthiness of a prospective customer, 76.5 percent industries refer to fellow firms already dealing with the customer. In Auto-parts industry 90 per cent units followed by Others industry 81.4 per cent, Garments industry 77.5 per cent, Electronics Industry 76.7 per cent, Rubber & Plastics industry 71.4 per cent, and in Metal Products 66.7 per cent units are using this method.

8.8 per cent industries in the small sector are referring to the bankers for information regarding prospective customer. This method of measuring creditworthiness of customer is used in Garments, Others, Auto-parts, Electronics, Rubber and Plastics and Metal Products industries by 12.5 per cent, 11.6 per cent, 10 per cent, 8.3 per cent, 7.1 per cent and 2.6 per cent units respectively.

By remaining 14.7 per cent industries in the small-scale industries other methods are used for measuring creditworthiness of the customer. In Metal Products industry maximum 30.7 per cent units are using other methods, Electronics industry 15 per cent, Garments industry 10 per cent and Others industry just 7 per cent units are using other methods.

Factors Influence Credit Policy

There may be various factors which influence the credit policy of a firm. But out of these two most important factors which influence the credit policy in small-scale industries are competition and customs and traditions in the industry.

In small-scale industries 52.7 per cent industries are deciding the terms and conditions of their credit sale according to the terms and conditions of other competitors. In Rubber & Plastics industry 62.5 per cent units closely followed by Metal Products industry 61.6 per cent, Electronics industry 58.3 per cent, Others industry 51.2 per cent,
Auto-parts industry 42.5 per cent, and in Garments industry 40 per cent units are framing their credit policies by keeping in mind the competition in the industry.

In small scale sector the other factor customs & traditions in the industry is also very important in deciding the credit terms. In 47.3 per cent industries credit policies are framed according to the customs and traditions of the industry. This practice is mostly followed in Garments industry (60% units). In Auto-parts industry also majority of units (57.5%) are following customs and traditions of the industry for framing credit policies. In Others industry 48.8 per cent followed by Electronics industry 41.7 per cent, Metal Products industry 38.5 per cent, and in Rubber & Plastics industry 37.5 per cent units are deciding the terms of credit sales according to the customs and traditions of the respective industry.

**Inventory Management in Small Scale Industries**

In small-scale industries inventories represent a very significant portion of total assets. Hence the importance of inventory management cannot be overemphasized. There are two basic questions relating to inventory management: (I) What should be the size of the order? (ii) At what level should the order be placed? The financial managers should aim at an optimum level of inventory on the basis of the trade-off between cost and benefit, to maximise the owner’s wealth.

**Inventory Control Techniques**

(i) **ABC Analysis Technique**

The ABC system is widely used classification technique to identify various items of inventory for purposes of inventory control. But in small-scale industries under study only 2 per cent industries are using ABC analysis technique. More than 96 per cent industries are not having separate department for controlling stores. And only 20 per cent industries appoint separate person to look after the inventories.

(ii) **Economic Order Quantity Technique**

The Economic Order Quantity may be defined as the level of inventory order that minimise the total cost associated with inventory management. In small-scale industries
due to the problem of finance, storage, and requirement only 10 per cent units are using this technique. The maximum is the percentage (20.9) of Others industry using E.O.Q. technique followed by Rubber and Plastics industry (12.5%), Garments industry (7.5%), Electronics industry (6.7%) and Auto-parts industry (5%).

(iii) Other Techniques

In small-scale industries 39.7 per cent industries are using the minimum level technique to avoid the stoppage of production due to non-availability of material. Except in Garments and Metal Products industries where just 16.30 per cent and 19.3 per cent respectively are using this technique of inventory control in remaining industries, this technique is very popular and 46.7 to 62.5 per cent units are using it.

On the other maximum level technique of inventory control is not very popular in small-scale industries due to the unstable demand of the product in the market. Only 14 per cent industries are using this technique. Maximum level technique is used more in Electronics industry where its percentage is 20 followed by Others industry 18.6 per cent, Auto-parts industry 15 per cent, Rubber & Plastics industry 10.7 per cent, Metal Products industry 10.3 per cent. In Garments industry only 10 per cent units are fixing the maximum level of stock to be kept at a time.

Re-order level technique is used just by 4.3 per cent industries in small sector. In Garments industry 11.2 per cent, in Electronics industry 3.3 per cent, and in Auto-parts industry 2.5 per cent are using it. In remaining industries it is not used at all.

(iv) No Technique

In 32 per cent industries, in small sector, are not using any technique of inventory control. Most of Metal products units (66.6%) are not using any technique of inventory control followed by Garments industry (55%), Electronics industry (23.3%), Rubber and Plastics industry (14.3%), Auto-parts industry (10%) and Others industry (7%). Most of these are small units in the industry.

Purchase Procedure in Small-scale Industries

In small-scale industries the purchase procedure of raw-material is different from large-scale industries. In small industries raw material is purchased by owners, either by
making personal visit to the vendor or by making conversation on telephone. This method of purchasing raw-material is adopted by 90 per cent units in Garments industry followed by Auto-parts industry where 85 per cent units, Rubber & Plastics industry where 82.1 per cent units, Metal Products industry where 79.5 per cent units, Electronics industry where 78.3 per cent and Others industry where 69.8 per cent units are using this method.

In extreme big units of small sector where the quantity to be purchased is large, other methods such as inviting quotations or tenders for supplying raw-materials are used. But their percentage is just 16 per cent and 3.8 per cent respectively. Tender method is adopted maximum (7%) by Others industry. In Garments and Auto-parts industries no one is using this method. In remaining industries just 3 to 5 per cent are using it.

Purchase of raw-material through inviting quotations is comparatively more popular in large units of small sector. In others industry 23.2 per cent, followed by Electronics industry 16.7 per cent, Metal products industry 15.4 per cent, Auto-parts industry 15 per cent, Rubber and Plastics industry 14.3 per cent and in Garments industry 10 per cent are using this method.

Store Organization in Small-scale Industries

The bin cards and store ledgers are the two main records which are kept to record the various items of the stores. In small-scale industries only 33.3 per cent industries are using bin system for store organization. In small sector only big units are using this system. Due to big size of units in Auto-parts industry 75 per cent units are using bin card system for store organization. In Garments industry 35 per cent units followed by Electronics industry 26.6 per cent, Others industry 22.1 per cent, Rubber and Plastics industry 21.4 per cent, and least in Metal Products industry 10.3 per cent units are using it.

According to the nature of raw material used in small-scale industries 43.5 per cent industries are using other methods of store organisation. In Electronics industry other methods are being used maximum by 56.7 per cent units followed by Garments industry (52.5%), Metal Products industry (48.7%), Others industry (37.2%), Rubber and Plastics industry (35.7%) and Auto-parts industry (20%).
Rest in 28.2 per cent industries mostly small units are not using any system at all for store organisation. The percentage of such units is minimum in Auto-parts industry just 5 per cent. In Garments industry, 12.5 per cent units, which are mostly engaged in tailoring job do not use any system of store organisation. In remaining industries percentage of such units range from 40 to 42.9.

**Pricing of Raw-Materials in Small-scale Industries**

There are several methods which can be used for pricing inventories used in production. But in most of the small-scale industries (65.2%) Average Cost method is used. Because in small-scale industries the identity of different lots of materials is lost when they are received in store due to the problem of space and not using bin card system for store organization. In Metal Products industry 83.3 per cent units, followed by Garments industry 80 per cent, Rubber & Plastics industry 66.1 per cent, Others industry 65.1 per cent, Electronics industry 41.7 per cent and in Auto-parts industry 35 per cent units are pricing their materials at the average cost.

On the other hand only 24.5 per cent industries are using FIFO method for pricing of materials issued from store. In this category these are mainly those units which are maintaining proper records of inventory. This method is adopted maximum in Auto-parts industry by 60 per cent units, followed by Electronics industry 36.7 per cent, Others industry 23.3 per cent, Rubber and Plastics industry 21.4 per cent, Garments industry 15 per cent, and in Metal Products industry just by 10.3 per cent units.

**V. FINANCIAL LEVERAGE AND CAPITAL STRUCTURE**

**Financial Leverage in Small-scale Industries**

Financial leverage refers to the use of fixed charge or fixed cost funds along with equity in the hope of increasing the return to the equity share capital. In small firms all the decisions are taken by the owner. And most of the businesses are owned by such persons who are not having any formal education of commerce/business. So, the question arises that whether before taking a decision to employ financial leverage its effects are considered or not. In 90 per cent of small-scale industries the owners and/or management do not even know the meaning of the term ‘financial leverage’. So, in 92.5 per cent
industries while employing financial leverage its effects are not considered. In small-scale industries the most important reason for not considering the effects of financial leverage is the limited choice between Debt or Equity. In small sector equity capital is in scarcity and when finance is required the only choice left is debt. In small sector only those industries are considering the effects of debt capital which have an option among equity or debt and with the help of experts study the options in detail before taking a financing decision. So, due to these reasons in small sector only 7.5 per cent industries are considering the effects of financial leverage. In Auto-parts industry maximum 12.5 per cent units, followed by Others industry 9.3 per cent units, Rubber and Plastics industry 8.9 per cent units, Garments industry 7.5 per cent units, Electronics Industry 6.7 per cent units and in Metal Products industry just 3.8 per cent units are considering the effects of debt capital.

**Considerations in Financing Decisions in Small-scale Industries**

There are various considerations that must be recognised in determining that which financing plan should be accepted by the company: (a) Trading on the Equity, (b) Debt-Equity Ratio, (c) The ability to cover fixed financing charges and (d) Non-financial Influences of the Financial mix.

In small-scale industries while taking the financing decisions 79.3 per cent industries do not consider Trading on Equity, Debt-Equity Ratio and Interest Coverage Ratio. Trading on Equity is considered just by 0.5 per cent industries while taking financing decision and all these industries belong to Others category of industries. Debt-Equity Ratio is considered only by those industries which have an option between Equity and Debt as a source of finance. And their percentage is just 2.7. In Others industries maximum 7 per cent units are using Debt-Equity Ratio followed by Auto-parts industry (5%), Rubber & Plastics industry (3%), and Metal Products industry (1.3%). Interest coverage Ratio is also very important tool in taking a financing decision, which is also not paid much attention by small-scale industries. In small sector only 17.5 per cent industries are using Interest Coverage Ratio for financing decisions. In this category the leading one is Electronics industry where 26.7 per cent units are considering it followed
by Garments industry (22.5%), Auto parts industry (20%), Rubber & Plastics industry (16%), Others industry (14%), and Metal Products industry (9%).

In small-scale industries non-financial factors play an important role in financing decisions. That is why 79.3 per cent industries take financing decisions on the basis of non-financing factors. In Metal Products industry 89.7 per cent units consider non-financial factors for financing decisions followed by Rubber & Plastics industry (80.3%), Garments industry (77.5%), Others industry (76.7%), Auto-parts industry (75%), and Electronics industry (73.3%). The main reason of it is non-availability or limited availability of equity in small sector.

**Consideration of Cost of Debt in Small-scale Industries**

The cost of debt or capital is a very important aspect of financial management but in small firms due to its difficulty in computation this concept is less important. In small-scale industries just 5.3 per cent industries are calculating cost of debt while taking a loan. In Auto-parts industry maximum 7.5 per cent units, followed by Others industry 7 per cent, Electronics industry 6.7 per cent, Rubber and Plastics industry 5.4 per cent, Garments industry 3.7 per cent, and in Metal products industry just 2.6 per cent units are considering cost of debt.

**Capital Structure Planning in Small-scale Industries**

Capital structure refers to the mix of long-term sources of funds and equity share capital including reserves and surpluses. In small-scale industries only big units are planning their capital structure particularly having a company form of organisation. Because, in small units owners/management do not have the proper knowledge of capital structure planning and they can not afford to hire the services of experts or do not have much choice among debt and equity to finance the future projects. These are the main reasons that in small-scale industries 94.7 per cent industries are not planning their capital structure. Only the biggest units of the industry (5.3%) are planning capital structure. That is why in Auto-parts industry maximum 7.5 per cent units are planning properly their capital structure whereas in Metal Products industry minimum just 2.6 per cent units are planning capital structure.
Use of Theories of Capital Structure in Small-scale Industries

In small-scale industries theories of capital structure are used only by 5.3 per cent industries which are planning their capital structure. And all these industries are using traditional theory of capital structure planning advocated by Ezra Solomon. These industries believe that a judicious use of debt increase the value of the firm and reduce the cost of capital. The optimum capital structure is the point at which the value of a firm is the highest and the cost of capital the lowest.

Debt-Equity Ratio of Small-scale Industries

In small-scale industries 51.5 per cent industries are using more than 200 per cent external equities in comparison to Owner(s)'s equities. In smaller units this percentage is more. In Metal Products industry maximum 62.8 per cent units are using more than twice external equities in comparison to internal equities, followed by 26.9 per cent units using 161 to 200 per cent, 7.7 per cent units using 121 to 160 per cent, and remaining 2.6 per cent units are using 81 to 120 per cent external equities of internal equities. In Auto-parts industry 45 per cent units are using more than 200 per cent external equities followed by 22.5 per cent units using 81 to 120 per cent external equities, 17.5 per cent units using 121 to 160 per cent, and rest 7.5 per cent units are using just 41 to 80 per cent outsiders' money in comparison to owner’s funds. The small-scale industries which are using less than 40 per cent external equities are just 2 per cent and which are using 41 to 80 per cent outsiders’ money their percentage is also very low i.e. 4.7 per cent industries. In Electronics industry minimum 38.3 per cent units are using more than 200 per cent external equities. In Garments, Others and Rubber & Plastics industries 45 per cent, 54.6 per cent and 58.9 per cent units respectively are using more than twice the external equities. Which shows that the majority of small-scale industries mainly depend on outsiders for survival.

VI. CAPITAL BUDGETING

Capital Budgeting in Small-scale Industries

Capital budgeting deals exclusively with major investment proposals which are essentially long-term projects and is concerned with the allocation of firm’s scare
financial resources among the available market opportunities. So, it is very important for every firm whether it is small or large. But in small-scale industries this important technique is used by a very limited number of industries. There are various reasons of not using this important technique for taking capital decisions in small sector. That is why in small-scale industries only 10.5 per cent industries are preparing capital budgets for taking long-term investment decisions. And these are big units in small sector which can afford the services of experts required for properly preparing capital budgets.

On the other hand 89.5 per cent industries in small sector take investment decisions without preparing proper capital budgets. In this category mostly are small units, which do not invest major amount in fixed assets after once they start business or make capital investment just by considering some aspects of capital budgeting. In it the maximum percentage is of Metal Products industry where 94.9 per cent units do not prepare capital budgets. In remaining industries 88.4 to 91.7 per cent units are not preparing any proper capital budgets for long-term investments.

In Auto-parts industry maximum 20 per cent units are preparing proper capital budgets for capital investment decisions followed by Rubber & Plastics industry (12.5%), Others industry (11.6%), Garments industry (10%), Electronics industry (8.3%), and Metal Products industry (5.1%).

**Who Prepares Capital Budgets in Small-scale Industries**

Capital budgeting involves the generation of investment proposals, the estimate of cash flows and their evaluation ranking of proposals on project evaluation methods basis, and finally continuous re-valuation after their acceptance.

In small-scale industries as explained earlier only 10.5 per cent industries are preparing capital budgets for long-term investment decisions. In all these 10.5 per cent industries capital budgets are prepared by a committee comprising both the owner(s)/management and experts. Experts may be an economist, management accountant, financial expert, tax expert, mathematician and the marketing and technical executives. Because in small firms it is financially not viable to have all these personnel
in the organization as permanent employees of the firm, so, their services are hired when the need of capital budgeting arises.

Priority of the Projects Fixed in Small-scale Industries

Classification of "Projects" according to priority is of greater benefit to smaller companies, since they usually have a constant capital rationing problem. Such a classification system will greatly aid management in selecting investments that will provide continuity to the firm's life.

In small-scale industries out of those 10.5 per cent industries which are preparing proper capital budgets for long-term investment decisions 69 per cent industries are fixing priority of the projects on the basis of postponable or not postponable categorization of projects. In Others and Electronics industries maximum 80 per cent units are fixing priority of projects followed by Garments industry (76%), Auto-parts industry (62.5%), Rubber and Plastics industry (57.1%), and Metal Products industry (50%).

On the other hand 31 per cent industries which are preparing capital budgets consider only one project at a time on the basis of its profitability. So, the question of fixing priority of the projects does not arise. In this category, the maximum percentage is of Metal products industry (50%) followed by Rubber & Plastics industry (42.9%), Auto-parts industry (37.5%), Garments industry (25%), and Others industry (20%).

Projects Evaluation in Small-scale Industries

A number of alternative capital expenditure proposals compete for allocation of funds. The main task is to rank the different proposals, delineate the funds for each and then take the decision. There are several method of project evaluation developed on several basis. But in small-scale industries all the 10.5 per cent industries which are preparing capital budgets are using traditional method for appraisal of the projects. In traditional method-Average Rate of Return technique is most popular among small firms for evaluating proposed capital expenditure. In small sector 85.7 per cent industries are using this technique while making capital budgets for evaluation of projects. In Electronics industry and Rubber & Plastics industry 100 per cent units are using this method whereas in Auto-parts industry 87.5 per cent units followed by Others industry
(80%), and Garments & Metal Products industries (75%) are using this method of project evaluation. The main reason of using this method by most of the industries in small sector is its simplicity in use and to understand.

On the other hand the remaining 14.3 per cent industries in small sector are using other traditional method – Payback Method. This method is used maximum in Garments and Metal Products industries by 25 per cent units followed by Others industry (20%), Auto-parts industry (12.5%) for project evaluation.

**The Post-Audit in Small-scale Industries**

An important aspect of the capital budgeting process is the post-audit, which involves: (1) comparing actual results with those predicted by the project’s sponsors, and (2) explaining why any differences occurred.

Post-audit is not very common in small firms which are using capital budgeting technique for long-term investment decisions. In small-scale industries out of 10.5 per cent industries which are preparing capital budgets only 9.5 per cent industries are using post audit technique to compare the actual results with those predicted by the project’s sponsors. On the other hand 90.5 per cent industries are not using post-audit technique or we can say, are not looking backward once the capital budgets are prepared. In Electronics, Metal-products and Rubber & Plastics industries not even a single unit is doing post-audit of the projects. In Garments and Auto-parts industries only 12.5 per cent units and in Others industry 10 per cent units are reviewing their projects in small sector.

**VII. SOURCES OF FINANCE**

**Short-term Capital in Small-scale Industries**

Short-term financing plays a vital role in the financing of assets, regardless of the size of the firm. However, this source is of particular significance to the small business.

In small-scale industries 90.3 per cent industries depend on short-term borrowings for their short-term needs of finance. Out of them 93.9 per cent industries approach commercial banks for short-term loans. In Garments, Electronics and Rubber & Plastics industries 100 per cent of the units which required short-term finance from outside, have
taken short-term loans from commercial banks. In Others industry, Auto-parts industry and also Metal Products industry 92.5 per cent, 88.2 per cent, and 83.3 per cent have approached banks for short-term financing. Only 6.1 per cent industries in small sector have taken short-term loans from friends and relatives out of 90.3 per cent small industries using short-term loan capital. So, we can say that commercial banks play the most significant role in providing working capital finance to small firms.

**Term Loans in Small-scale Industries**

Small-scale industries find it difficult to secure adequate finance from institutional sources even for their working capital requirements because of their own inherent limitations, on the one hand and the generally high standards applied by the lending institutions to borrowers, on the other. These are the main reasons that out of 72.7 per cent small industries which have taken term loans for investment in Plant & Machinery, land & building or permanent addition to current assets, 74.6 per cent industries have taken term loans from commercial banks. And just 10 per cent big units in the small sector which could fulfill the stringent terms and conditions of financial institutions have taken loans from them. Remain 15.4 per cent industries have taken term loans from non-financial institutions (friends, relatives and money lenders). In small sector bank financing is most popular. But bank also provide medium or long-term loans against the security of land or building or against the security of plant & machinery to be purchased. So, the smaller units which can not provide any such security cannot get term loans even from commercial banks. These smaller units depend on friends and relatives or money lenders.

In Metal Products industry the percentage of units which have taken term loans from commercial banks is maximum (78.2%) closely followed by Rubber and Plastics industry (77.3%), Electronics industry (75%), Auto-parts industry 73.3 per cent), and Others industry (73%). In Garments industry minimum 70.8 per cent units have taken term loans from banks.

As far as other financial institutions are concerned which have provided term loans to small sector the percentage of units (16.7%) is maximum in Auto-parts industry closely followed by Electronics industry with 15 per cent and Garments industry with
14.6 per cent. In remaining industries just 5 to 9.4 per cent units have taken term loans from other financial institutions.

From friends and relatives or money lenders in Others industry category maximum 17.6 per cent units have taken term loans. In remaining industries except Auto-parts industry (10%) 14 per cent to 16.4 per cent units have taken loans from friends, relatives or money lenders.

The remaining 27.3 per cent industries have no term loans. In it most of them are small units, which are financially sound or amount of fixed assets required is not huge and if loan was taken it has already been repaid. These are 40 per cent units in Garments industry followed by 33.3 per cent units in Electronics industry, 29.5 per cent units Metal Products industry, 25 per cent units in Auto-parts industry, 21.4 per cent units in Rubber & Plastics industry, and least 14 per cent units in Others industry.

**Long-term Financing in Small-scale Industries**

In small-scale industries due to their nature of organisation owners’ funds are in short supply. Because their limited access to the market. So, for long-term financing they mainly depend on term loans. As discussed earlier in small sector 72.7 per cent industries have taken term loans for expansion, modernization or even for starting business.

**Loan Capital in Small-scale Industries**

Out of these 72.7 per cent industries 26.5 per cent industries have taken more than 75 per cent loans of total capital of the firm. In this category the percentage of Rubber & Plastics industry is maximum (41%) followed by Others industry (34.9%), Electronics industry (30%), Metal Products industry (21.8%), Auto-parts industry (20%), and Garments industry (12.5%).

21 per cent industries in small sector are using more than 50 per cent but less than 75 per cent loan capital. In it the Auto-parts industry is leading one with 40 per cent followed by Metal Products industry (28.9%), Others industry (20.9%), Garments
industry (20%), Electronics industry (16.7%), and least one is Rubber and Plastics industry with just 3.6 per cent units.

Other 7.7 per cent industries in small-sector are using more than 25 per cent but less than 51 per cent loan capital. In this category the maximum percentage (10.2%) is of Metal Products industry closely followed by Others industry (9.3%). In remaining industries the percentage varies from 5 to 7.5 per cent.

In the other category we have included those industries which are using just upto 25 per cent loan capital. In it the Rubber & Plastics industry is having maximum per cent of units (28.6%). In Others industry & Garments industry the percentage of units is 20.9 and 20 respectively. In remaining industry from 10 to 13.3 per cent units are using less than 26 per cent loan capital.

In remaining 27.3 per cent industries in small sector no loan capital is used. In this mostly are smallest units which required small amount for investment in plant and machinery, in land & building or which are old units had already repaid the loan capital. In it the maximum percentage is of Garments industry (40%) followed by Electronics industry (33.3%), Metal Products industry (29.5%), Auto-parts industry (25%), Rubber and Plastics industry (21.4%), and the least in Others industry (14%).

**Owners’ Capital in Small-scale Industries**

In small-scale industries 27.3 per cent industries are using only owners’ funds for long-term financing. These are mainly small units or old well established units. In Garments industry maximum 40 per cent units (mainly those engaged in tailoring work) are using 100 per cent owners’ capital for long-term financing followed by Electronics industry (33.3%), Metal Products industry (29.5%), Auto-parts industry (25%), Rubber & Plastics industry (21.4%), and least in Others category of industry 14 per cent units.

Next 17.5 per cent industries in small sector are using more than 74 per cent but less than 100 per cent owners’ capital for long-term financing. In it the maximum percentage (28.6%) is of Rubber & Plastics industry followed by Others industry (20.9%), Garments industry (20%), Electronics industry (13.3%), Metal Products industry (10.3%), and Auto-parts industry (10%)
In small sector just 7.7 per cent industries are using 50 to 74 per cent owners’ funds. The percentage of various industries in this category ranges from 5 to 10.2 per cent. Other 21 per cent industries in small sector are using owners’ capital for long-term more than 24 per cent but less than 49 per cent of total capital. In it the Auto-parts industry is leading one with 40 per cent units. In Metal Products industry, Others industry and Garments industry 28.2 per cent, 20.9 per cent and 20 per cent units respectively are also using owner’s capital between 25 to 49 per cent of total capital. In remaining two industries Rubber & Plastics and Electronics just 3 to 6.7 per cent units are using 25 to 49 per cent owners’ capital.

Rest 26.5 per cent industries of small-scale industries are using less than 25 per cent owners’ capital in long-term financing. In Rubber and Plastics industry maximum 41 per cent units followed by Others industry 34.9 per cent units, Electronics industry 30 per cent units, Metal Products industry 21.8 per cent units, Auto-parts industry 20 per cent units, and Garments Industry 12.5 per cent units are in this category.

CONCLUSIONS AND SUGGESTIONS

I. PLANNING FUNCTION

In the dynamic small-scale industries, the planning function is given very little consideration. As the study shows, only 39.3 per cent industries are properly making plans for the future. On the other hand, 42.7 per cent industries are formulating plans in unwritten form without determining operating policies and strategies. This shows the casual approach of the managers of the small firms towards the important function of planning.

Planning is absolutely essential if the firm is to operate efficiently and effectively. To accomplish this function in the most efficient manner we recommend that planning should be made in writing and include the following steps or phases:- (1) establishing the objectives of the firm, (2) formulating strategies, (3) determining operating policies, and (4) creating procedures. While each of these steps is separate and distinct, they are interrelated.
In small-scale industries 80 per cent units gave response in 'yes' to the question “Do you make financial plan?” But when we discussed the preparation of financial plan in detail, the facts were revealed that only very few of them are properly making financial plans. Out of them mostly are large units which can hire the services of experts for financial planning. In small industries, financial planning is mis-understood by most of them. To them it means making arrangements for funds.

The financial plan of a firm should be formulated in the light not only of present but of future developments as well. It should take into consideration the present capital needs for fixed assets, working capital, probable earnings, and requirements of investors; and it should anticipate possibilities of later expansion, combination with other firms, higher or lower future interest rates etc.

To make an effective financial plan in small industries the help of experts should be taken.

In the small-scale industries under study, majority of the units are making profit plans. But to most of them profit planning mean just estimating future profits on the basis of past experience. This is clear from the fact that the use of tools like Break-even analysis in profit planning has been resorted to only by 1/5th of the respondents.

There are two key elements in predicting a company’s profitability: Sales and the related costs and expenses. In small sector 67.7 per cent industries forecast their sales. Most of them are using judgement based method for sales forecasting. And 60 per cent industries are forecasting expenses.

In using the judgement or subjective approach, we should remember the historical sale data, combined with the assumptions about the external and internal environment, serve as the foundation.

For forecasting expenses requires that we understand the basic nature of the firm’s expenses. Expenses may be classified in terms of fixed and variable, or some combination of both.
Profit planning should represent an overall plan of operations, covering a definite period of time, and formulating the planning decisions of management. It should consist of the operating budget, the financial budget and the appropriation budget.

Effective profit planning cannot be carried out in a casual manner as is in small industries and should emerge from a rigorously disciplined examination of all aspects of business and alternative strategies which may become indispensable.

II. FINANCIAL INFORMATION SYSTEM

In the small-scale industries under study most of the units are maintaining proper books of accounts. But in most of them, accounts books are maintained for the purpose of fulfilling the legal requirements of various government agencies and not for providing valuable financial information for financial decisions. This is the reason that only 6.5 per cent industries, mainly large units, working under the organisation of company (as a Pvt. Ltd. or Public Ltd. Company) are having separate department for accounts. In other industries mostly appoint part-time person(s) for maintaining books of accounts.

The basic elements in designing a viable accounting system should include the following:

1. Classifying and summarising data for the purpose of accessing the current position of the business.
2. Maintaining adequate control of corporate operations
3. Providing suitable financial statements for use by prospective creditors and by management.
4. Developing information essential to determining future course of action, that is, planning.

The entrepreneur – executive who knows that he or she does not possess the expertise necessary for establishing a strong system, if the resources of business permit, a qualified full-time internal accountant should be employed.
Due to comparatively more competition in small-scale industries it becomes necessary to use some techniques of cost control in small firms for survival. But in small sector, only 10 per cent big units are using cost reduction techniques.

In order to reduce the cost of production the owner / management in small-scale industries should continually scrutinise products, processes, procedures, organisation, methods and personnel to improve efficiency and reduce costs.

To ensure that cost reduction scheme works well, a Cost Reduction Committee may be formed to formulate a detailed plan. It is essential to obtain co-operation from all levels to determine the priority of actions, methods to be employed in carrying out the investigation and finally to take steps for implementing the recommendations. By continuous follow-up the cost reduction plan will be successful.

Only one-third industries in small sector are preparing Funds Flow / and Cash Flow Statements to analyse the main sources and applications of funds and cash generated as well as used during the accounting year. These statements are mainly prepared by partnership firms or companies. Comparative statements are also prepared by the same number of industries. In most of the industries the purpose of preparing comparative statements is inter-period comparison.

In India, though the statements of changes in financial position has not so far become a part of the financial reporting of a large number of companies, but, banks and financial institutions require it when a company approaches them for loans.

Information concerning the financing and investing activities of a business enterprise and changes in its financial position for a period is essential for financial statement users, particularly owners and creditors, in making economic decisions. So, a statement summarising changes in financial position should also be prepared as a basic financial statement for which an income statement is prepared.

In small industries only one-fifth units are preparing income and expenditure budget.
Internal control has long been recognised as important system in the large companies. But in small industries maintaining internal control is difficult. This is the reason that only 7 per cent industries in small sector, under study, apply a properly developed system of internal control.

Internal control plays a key role in enhancing the quality of the financial output employed in the decision-making process. Although this applies to all businesses, whether large or small, an extra dimension exists for the small firm in which the owner has invested a large portion of his or her net worth. A faulty decision for this individual can materially impact an entire lifestyle for many years, if not for a life time. Accordingly, having valid and timely inputs in the form of accounting information is essential thereby minimizing the probability of poor judgements.

A company regardless of size may implement procedures that expedite a sound accounting structure. These guidelines should include, but not be limited to, the following:

1. Record all cash receipts immediately.
2. Deposit all cash receipts intact daily.
3. Make all payments by serially numbered cheques, with the exception of small disbursements from petty cash.
4. Use an imprest petty cash fund entrusted to a single custodian for all payments other than by cheque.
5. Reconcile bank accounts monthly, and retain copies of the reconciliations in the files.
6. Use serially numbered purchase orders for all purchase transactions.
7. Maintain a receiving record, preferably by means of serially numbered receiving reports.
8. Issue cheques to vendors only in payment of approved invoices that have been matched with purchase orders and receiving reports.
9. Prepare serially numbered sales invoices for all shipments to customers.
10. Prepare and mail customers' statements monthly.
11. Balance subsidiary ledgers with control accounts at regular intervals.
12. Prepare comparative statements monthly in sufficient detail to disclose significant variations in any category of revenue or expense.

In small-scale industries, even today, cost accounting is considered useless. It is clear from the study that only 4 per cent industries are maintaining cost accounts properly.

Procedures for affording information regarding the cost of providing a unit of product or service can be instrumental in sound planning and control for any company, regardless of its size. The owner of the small enterprise should investigate the feasibility of cost accounting. If the system is initiated, the executive of the small operation has a strong need for understanding the cost accounting procedures. In an environment stipulating a thorough knowledge of most facets of the company, as is the case for most small entrepreneurs, cost data are particularly meaningful.

In small industries competition plays the major role for price determination. Majority of units in small sector fix prices of their product by keeping in mind the competition prevailing in the industry. And only one-fourth industries adopt cost-base method for price determination.

In fixing price of product or services, the owner / management has to be clear on the company’s marketing objectives and on the target market.

It may be mentioned that as price is an element in the market mix, each firm should develop a strategy to enable it to achieve its marketing objectives in the target market.

The three elements on which considerations should be given in a pricing strategy are:

(1) Cost
(2) Demand
(3) Competition.

To obtain maximum benefits it is desirable to consider the above three elements simultaneously.
III. WORKING CAPITAL MANAGEMENT

The management of working capital is one of the most, if not the most, important duties of manager of the small firm. But we found in the study that only 57.3 per cent industries in the small sector are planning working capital well in advance. Other industries start thinking of making arrangement of working capital when the need arise.

For working capital, in small-scale industries, most of the units depend on commercial banks. And, only 15.3 per cent industries arrange working capital on their own or with the help of friends/relatives or by getting advances from customers.

To estimate the working capital needs of a firm, we should study the factors which affect the need for working capital – the terms offered by supplies, the terms offered to customers, the average period of lead time for various inventory terms, the seasonal fluctuations in sales, the production cycle, the level of stock and other influencing factors. These factors may be used to relate the balance sheet items to sales volume. The relationship yield measures which may serve, among other things, as tools for the prediction of future working capital needs.

Cash budget is an important tool of efficient cash management. It serves both as a planning tool and a control device. But in small-scale industries only 38.2 per cent industries are using this tool for efficient cash management. No separate department is there in most of the small industries for this purpose. Cash matters are mainly looked after by the owner(s). Even cash discount technique is used for speedy collection of cash by only 18.3 per cent industries.

Planning for cash requirements is an essential management function of any business concern. It is not enough for an undertaking to make a profit. Cash resources should be planned to finance a cash flow, without which otherwise efficient and profitable business have encountered financial difficulties.

The owner/financial officer should plan his cash and credit sources in such a way that the normal operations of the firm are not disrupted by a shortage of cash and that opportunities for capital expenditure are not lost because of an inability to finance them.
A proper cash management necessitates the development and application of some practical administrative procedures to accelerate the inflow of cash and to improve the utilisation of excess funds. These practical administrative procedures include:

1. Planning of cash requirements;
2. Effective control of cash flow; and
3. Productive utilisation of excess funds.

In small-scale industries the period of credit sales varies according to the value of the product. In small firms maximum number of units (37.5 per cent) are granting credit for an average period of 31 to 50 days closely followed by 36.7 per cent industries which are selling goods for an average credit period up to 30 days. 18.5 per cent industries are granting credit for 61 to 90 days and remaining 7.3 per cent for 91 to 120 days. No unit in small sector is granting credit for more than 120 days. Cash discount technique is not very common in small industries to reduce their receivables.

In small sector, to measure the creditworthiness of a prospective customer, two-third industries refer to fellow firms already dealing with the customer. 8.8 per cent industries refer to the bankers for information regarding prospective customer and remaining industries use other methods for measuring creditworthiness.

The terms and conditions of credit sales are decided by 52.7 per cent industries on the basis of competitors policy. In other industries credit policies are framed according to the customs and traditions of the respective industry.

While making a credit policy a firm should fix the basic criteria for the extension of credit to customers.

For effective management of credit, the firm should lay down clear cut guidelines and procedures for granting credit to individual customers and collecting individual accounts. The firm should follow the policy of treating all customers equal for the purpose of extending credit. Each case should be fully examined before offering any credit terms.
A collection policy should be made because all customers do not pay the firm’s bill in time. Some customers are slow-payers while some are non-payers. The collection efforts should, therefore, aim at accelerating collections from slow-payers and reducing bad-debt losses. A collection policy should ensure prompt and regular collection.

In small firms cash discount technique is not common for speedy collection of cash. This technique should be adopted for prompt payment of receivables.

In small-scale industries the important techniques of inventory control such as ABC Analysis and Economic Order Quantity are used only by a very few industries. Minimum level technique is used in approximately 40 per cent industries to avoid stoppage of production. In one-third of industries no technique is used for inventory control.

In small sector raw-material is purchased by the owner either by making personal visit to the vendor or by conversation on phone in most of the industries. In large units of the sector where huge quantity of raw-material is purchased, other methods of purchasing such as inviting quotations or tenders are used.

For store organisation Bin Cards system is used only by one-third industries in small sector. And these are mainly large units. According to the nature of raw-material used in small industries, 43.5 per cent units, are using other methods of store organisation. Out of 28.2 per cent units, mostly small units are not using any system at all for store organisation.

In small industries ‘Average Cost Method’ is used by majority of the units for pricing of materials issued from store. And First-in-First Out Method is used only by one-fourth units. Some units, which are not maintaining store ledger are not using any method for valuation of inventory.

As a first step in the inventory control process, the inventories should be classified into different types to determine the type and degree of control required for each. The ABC system is a widely-used classification technique to identify various items of inventory for purposes of inventory control. This technique is based on the assumption that a firm should not exercise the same degree of control on all items of inventory. It
should rather keep a more rigorous control on items that are (i) the most costly, and/or (ii) the slowest-turning, while items that are less expensive should be given less control effort.

On the basis of a trade-off between benefits derived from the availability of inventory and the cost of carrying that level of inventory, the appropriate or optimum level of the order to be placed should be determined. But in some cases it is quite possible that the deliveries from suppliers may be slower than expected for reasons beyond control and there may be an unusual and unexpected demand for stocks. So, to meet such contingencies, firms should keep additional inventories which are known as safety stocks.

Another important question pertaining to efficient inventory management is: When should the order to procure inventory be placed? To solve this problem, each firm should fix its reorder point.

In order to avoid over and under investments in materials, the management should decide the maximum and the minimum quantity of materials to be kept in store.

The store should be divided into several sections, each meant for one particular type of material. Each section should have suitable containers for keeping different varieties of that particular type of material. Each bin or rack should also be appropriately numbered and indexed for easy identification.

In small units of small sector at least store ledger should be maintained on the “perpetual inventory system”.

IV. FINANCIAL LEVERAGE AND CAPITAL STRUCTURE

In most of small-scale industries the owners and/or management do not know even the meaning of the term ‘financial leverage’. So, in 92.5 per cent industries while employing financial leverage its effects are not considered. In small firms the most important reason for not considering the effects of financial leverage is the limited choice between Debt or Equity.
In small industries while taking the financing decisions 79.3 per cent industries do not consider Trading on Equity, Debt Equity Ratio and Interest Coverage Ratio. Non-financial factors play an important role in financing decisions of these industries.

The cost of debt or capital is a very important aspect of financial management, but in small firms due to its difficulty in computation, this concept is less important. In small sector just 5.3 per cent industries are calculating cost of debt while taking financing decision. And these are mainly large units.

The small-scale industries should clearly understand the importance of the concepts of operating, financial and combined leverages. These concepts can be proved to be of great use in financial decision making in small-scale industries. If the operating risk, as measured by the operating leverage is high, it indicates that the firm should keep its financial risk low. And if the Operating risk happens to be low it would permit the company to take as much advantage of high financial leverage as possible. Hence it would increase the profits available to equity shareholders.

While taking a financing decision, the cost of capital is very important aspect, which is completely ignored in small industries. The main reason of it is, debt the only source of finance in majority of the small firms. The traditional and more sophisticated methods of determining the level of debt use in firm’s capital are not as applicable for small firms as they are for large companies, therefore, for small industries we recommend the use of the indifference point technique when using debt.

Capital structure refers to the mix of long-term sources of funds and equity share capital/owners’ capital including reserves and surpluses. In small-scale industries only big units are planning their capital structure particularly, those having a company form of organisation. Because, in small units owners/management do not have the proper knowledge of capital structure planning and they can not afford to hire the services of experts or do not have much choice among debt and equity to finance the future projects. These are the main reasons that in small sector 94.7 per cent industries are not planning their capital structure.
All the 5.3 per cent industries, which are planning their capital structure, are using traditional theory of capital structure planning advocated by Ezra Solomon.

In small sector majority of industries are using more than twice external equities in comparison to owner(s)'s equities.

Capital structure planning keyed to the objective of profit maximisation ensures the minimum cost of capital and the maximum rate of return to equity holders. The amount of capital a firm needs is not its only financial consideration. Equally important is the capital mix; the kinds of capital that form the company’s financial base. How much will be the equity money representing the funds owed by the stockholders in the enterprise? How much will be borrowed? How much will be raised by other means? A financial manager should determine the proper capital structure for his firm. He should determine the mix of debt and equity securities which would maximise the value of the equity stock.

The capital structure should be planned generally keeping in view the interests of the owners of the firm and financial requirements of a firm.

Generally the following factors should be considered whenever a capital structure decision has to be taken: (i) leverage effect on earnings per share, (ii) growth and stability, (iii) cost of capital, (iv) marketability, (v) cash-flow ability of the firm, (vi) control, (vii) flexibility (viii) size of the firm, and (ix) flotation costs.

V. CAPITAL BUDGETING

Capital budgeting deals exclusively with major proposals which are essentially long-term projects and is concerned with the allocation of firm's scare financial resources among the available market opportunities. So, it is very important for every firm whether it is small or large. But in small-scale industries this important technique is used just by 10.5 per cent industries for taking long-term investment decisions. And these are big units which can afford the services of experts required for properly preparing capital budgets. Remaining industries are taking investment decisions without preparing capital budgets.
For preparing capital budgets in above mentioned industries, a committee including both-owner(s)/management and experts is constituted. Out of 10.5 per cent industries, 69 per cent fix priority on the basis of postponable or not postponable projects.

All the industries, which are preparing capital budgets use traditional method for appraisal of the projects. In traditional method – Average Rate of Return technique is most popular in small industries – for evaluating proposed capital expenditure. The other method – Payback Method is used just by 14.3 per cent industries.

Post-audit is not very common in small firms which are using capital budgeting technique for long-term investment decisions. Approximately one-tenth of them are using post-audit technique to compare the actual results with those predicted by the project’s sponsors.

Capital budgeting is as complex and important to small firms as to large firms; therefore, it is essential that owner-managers adopt a formalised capital budgeting procedure. Although each firm must develop its own budgeting procedure, certain common elements should be taken into consideration by all firms. For example, a budget should be developed to cover a certain period (e.g., five years).

Decisions regarding investments should be made at the highest possible level for two vitally important reasons: (1) one bad decision may cause failure and (2) most small firms face a continuous capital shortage.

In deciding which projects to accept, managers of small firms should give high priority to projects that cannot be postponed as well as to those which improve operating efficiency. The timing of project generation should be continuous; however, to avoid less than optimal decisions, the evaluation process should be done at a specific time (e.g., quarterly, semi-annually, or annually).

There are several methods of project evaluation. Payback is an important technique but does not take into account the time value of funds in evaluating the return on a project after the investment is recovered. Average rate of return on average investment is an extremely weak technique and should not be used, even in conjunction with other methods. Internal rate of return and net present value consider the time value
of funds but are weakened by the fact that small industries normally do not have the capacity to determine the required rate of return (weighted average cost of capital) that may be used as an acceptance criterion. These weaknesses can be corrected by making certain adjustments to the internal rate of return concept. First, the capital account should be divided into debt and equity sources. Second, cash flows should be divided in such a way that management can calculate the IRR on debt and equity capital.

There are several methods of evaluating risk. It is suggested that the risk inherent in a project may be best observed by calculating the probability distribution of the firm’s cash flows.

The control process in the small industries, while much less complicated than in the large firms, is quite important. The owner-manager should follow the progress of projects from their approval until their completion. Also, management should measure actual performance with expected results. It is through this control process that future capital budgeting procedures will be improved.

VI. SOURCE OF FINANCE

In small-scale industries 90.3 per cent industries take short-term loans to fulfill their short-term needs of finance. Out of them most of the industries approach commercial banks for short-term loans.

In small sector 72.7 per cent units are using term loans for investment in plant and machinery, land & building or permanent addition to current assets. Out of them two-third industries have also taken term loans from commercial banks. And just one-tenth big units, which could fulfill the stringent terms and conditions of financial institutions, have taken term loans from them. Remaining units have taken the help of friends and relatives or money lenders.

In small sector, approximately one-fourth industries have not taken any long-term loans for long-term financing. These are mainly small units requiring less long-term investment and old and well established units. In remaining three-fourth industries, both-owners’ funds and external funds have been used for long-term financing. Out of them one-fourth are using more than three-fourth external funds for long-term financing. And
one-fifth of them are using between one-half to three-fourth external funds. Remaining one-fourth industries are using less than one-half external equities for long-term needs.

We see that most of the small industries are depending on commercial banks for their short-term and long-term needs of finance. But these banks are smaller one, whose field of activity is restricted to a small area. However, the resources of these banks are limited; and unless bigger banks take a promotional view in the initial stages and extend the much needed assistance to small industries, the later would be forced to borrow from non-institutional lenders, the disadvantages of which need no elaboration here.

There are some directions in which small-scale industries may improve their methods of operations, etc., and make their proposals acceptable to lending institutions. These are:

(i) It may not be usually possible for small industries to furnish financial and other data in a thorough and detailed manner. In such cases, as much information as is available on the following aspects of the concern may be given to the lending institutions.

(a) Details of the nature of the industry and its products;
(b) Data regarding performance, estimated cost of production and selling price;
(c) Estimates regarding market prospects, capital invested, proportion of borrowed capita;
(d) Purpose of the loan, result expected from the investment, etc.

(ii) Concern should, in their own interest and in order to facilitate the assessment of loan proposals by lending institutions, try to maintain audit accounts.

(iii) The units must be able to produce acceptable evidence for verification of the value of assets offered as security.

(iv) Loans sanctioned should not be used for purposes other than those for which they have been advanced.
The particular importance and necessity of retained earnings to small firm as a means for building an equity base should be recognised.

GENERAL SUGGESTIONS

There is a plethora of rules, regulations and procedures laid down by different government agencies for helping the small-scale industries in the country. As a result, it is very difficult to say at any given point of time as to the correct official/legal position with regard to objectives and methods of promoting the small-scale industries in the country. Therefore, a central legislation somewhat on the pattern of Japan or U.S.A. incorporating the objectives, methods and procedures for promotion and development of small-scale industries is the greatest need of the hour. This basic central law should also provide for a central agency just like Small-Business Administration in U.S.A.

The Central government as well as State government agencies responsible for small industry development should increasingly shift their attention from protective measures like price preference, cash subsidies etc. to strengthening the demand stimulating efforts and skills of the small-scale units.

Small enterprises must be developed along with large units. From the viewpoint of long-term perspective, however, the capacity of small manufacturers to become economically viable, technically progressive and efficient, and to develop competitive strength shall be the only justification for their continuance. In the intervening period, the Government should help create conditions to facilitate their smooth growth.

Small-scale enterprises in India must become technology-driven, and not depend on crutches like reservation and fiscal concessions. A complete overhaul of the small-scale policy is necessary. And it is the Indian entrepreneur and the consumer who will benefit the most.