CHAPTER X

THE CAUSES OF SICKNESS
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Industrial sickness in the country is growing at a fast pace, as can be judged from the number of units, which have gone sick during the past four years. According to information given in Parliament, there were 60,173 sick units at the end of December 1982.\(^{(1)}\) This figure went up to 64,388 units at the end of June 1983. The figure increased up to 92,015 at the end of December 1984. According to available data, there were in all about 12.75 lakh small scale units (both registered and unregistered) in the country as at the end of 1984-85. This means that 7.21 per cent of the units were sick. However in reality the actual number and percentage of sick and/or closed units may be much more than 7.21 percent. This is because the above figures are based on reporting made by commercial banks. It is likely that some units might be sick, but might not have been identified by the banks. The National Census of Small Scale Industries, 1972, reported that 38 per cent of the registered units (98,476 units) were either not traceable or permanently closed.\(^{(2)}\)

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\(^{(1)}\) The Financial Express dated 27.3.85.

During my survey, it was observed by me that out of 66 units, 15 units or 22.72 per cent of the units were sick. The percentage of sick units was found to be much more than the national percentage of 7.21. This may be due to the area selected or the comparatively small size of the sample chosen for the study. Amongst 66 units, the percentage of sick units was maximum in the 'Chemicals & Chemical Products' industry, where 4 units out of the 9 units or 44.4 per cent of the units were sick. The percentage of sick units was more in 'Basic Metal Products' industry also where 3 units out of 12 units or 25 percent of the units were sick. 'Light Engineering' category too had a higher percentage of sick units. In 'Engineering' industry, out of 22 units, 6 units or 27.29 percent of the units were found to be sick. But in the case of 'Electronics' industry and 'Food Industry' not a single unit was found to be sick.

Till the end of 1983 the total bank and institutional credit of Rs.3778.29 crores was locked up in 80,110 sick units comprising of small, medium & large scale industries. Such locked-up public money has been ominously growing from year to year, as is evident from the following figures.
It is revealed from the Report of Reserve Bank of India on Currency & Finance in India 1983-84 that out of the total of 64,388 sick units in the small scale sector involving bank finance of Rs.626.52 crores, about 80 per cent of the units are non-viable. Thus out of 64,388 sick small scale units, only 5983 units with outstanding credit of Rs.194.50 crores were considered by banks as potentially viable.

According to Annual Report 1984-85 of RBI as at the end of December 1984, there were 92,015 sick small scale units, involving bank finance worth Rs.879 crores. Out of 92,015 sick units, only 6242 were considered by banks as potentially viable. Commercial banks have granted nursing finance to 2228 sick units which were potentially viable.

It is true that the phenomenon of industrial sickness is a part of the process of industrialisation itself. But for a developing country like India, it poses a very difficult problem, particularly due to its adverse impact on capital as well as entrepreneurship.
What is a sick unit? Several definitions have been put forward as to what industrial sickness is. In simple terms, a sick unit is one which is not healthy. But then what is a healthy unit? According to Sudarshan Lal, any unit which assures a reasonable return on its capital and reserves, after providing for depreciation (3) (and reasonable remuneration for the proprietor or working partners in a partnership firm) is a healthy unit. According to Lal a reasonable rate of return on capital and reserves can be 9 percent to 16 percent per annum, considering interest rates on bank deposits and bank lending. The units which do not satisfy this criterion may be treated as sick.

As per the report of the Study Group of State Bank of India, 1975, a sick unit is one which fails to generate internal surplus on a continuing basis and depends for its survival upon frequent infusions of external funds.

Reserve Bank of India has laid down the following definition for classifying a unit as sick, which is being used by commercial banks for identifying sick units:

(3) Lal Sudarshan "How to Prevent Industrial Sickness" (Navrang, New Delhi) 1979, Page 174.
"A sick unit is that which has incurred a cash loss for one year and in the judgement of the bank, is likely to continue incurring cash losses for the current year as well as in the following year and the unit has an imbalance in its financial structure, such as current ratio is less than 1:1 and there is a worsening trend in debt-equity ratio"

A term lending institution's definition of a sick unit is as under:

(i) Continuous default in meeting four consecutive half yearly instalments of interest or principal in respect of institutional loans;

(ii) Continuous cash losses for a period of two years or continued erosion in net worth, say, by 50 per cent;

(iii) Mounting arrears on account of statutory and other liabilities for say a period of one/two years.

According to Section 72 A of the Income Tax Act 1961, a sick company is defined as:

"Amalgamating company which was not, immediately before such amalgamation, financially viable by reason of its liabilities, losses and other factors".

According to some, only such units may be considered sick in which a major part say 50 per cent of its equity and reserves is eroded by cash losses.

It appears that this definition has been accepted by the Finance Ministry, as in the Union Budget 1985-86, it is mentioned that the onus for reporting sickness will be laid on the managements of the units themselves who will be required to seek a fresh mandate from their share holders after 50 percent of the net worth of the company has been eroded.

T. Tiwari Committee (1984) defined a sick industrial undertaking as under.

"A sick industrial undertaking is one which has all the following characteristics and also those as have been taken over and continue to be so taken over under Industries (Development & Regulation) Act 1951, namely

(i) the industrial undertaking incurs in the immediate preceding accounting year cash loss as disclosed in the audited or the proforma balance sheet that is to say the loss arrived at in the manufacturing/profit & loss account of such industrial undertaking after making provisions for

(5) Lal Sudarshan "How to Prevent Industrial Sickness" (Navrang, New Delhi), 1979, Page 174.
all expenses, including interest as also accrued interest but without providing for any depreciation (in accordance with the provisions of Companies Act 1956) and transfers to reserves like Development Rebate Reserve, Investment Allowance, General Reserve etc.

(ii) the current ratio that is to say the ratio between current assets and current liabilities as disclosed in the audited or proforma accounts of the immediate preceding accounting year of such industrial undertaking proves adverse according to the prevalent commercial accounting practice; and

(iii) the accumulated losses of such industrial undertaking as at the end of the immediate preceding accounting year result in erosion of 50 percent or more of its net worth or in any erosion of its paid up capital.

According to "The Sick Industrial Companies (Special Provisions) Bill 1985" a sick industrial company means an industrial company (being a company registered for not less than seven years) which has at the end of any financial year accumulated losses equal to or exceeding its entire net worth and has also suffered cash losses in such financial year and the financial immediately preceding such financial year.
At this juncture I would also like to distinguish between sickness and bankruptcy. Prof. Altman (who was an adviser to the Presidential Congressional Commission on the National Bankruptcy Laws of the USA and Associate Professor of Finance, at New York University, and who has done pioneering work on 'Industrial Sickness') describes that in the case of insolvency one will not be able to pay bills when they are due. This can be temporary phenomenon. Similarly in the case of sickness, failure is there and in some cases firm's liabilities also exceed a fair valuation of its assets, and the company has a negative or declining net worth. But, actual declaration of insolvency has not been done. Whereas in the case of bankruptcy, the firm's liabilities exceed its assets, its net worth is negative and there is actual declaration of bankruptcy together with a petition by a company to a court to liquidate assets or to attempt some sort of a recovery programme. In bankruptcy a unit is always insolvent. In the case of sickness, a firm need not have become insolvent, but may be leading towards insolvency.

Most of the definitions of sickness given above are based on financial statements of a unit. But as we know submission or preparation of financial statements is many a time delayed and it is not possible for an entrepreneur or an outsider like the banker to depend on these statements for detecting sickness.
It is therefore necessary for an entrepreneur and a banker to judge sickness in a unit, based on certain symptoms. Let us mention briefly what such symptoms of sickness are.

**Symptoms or Signs of Sickness**

If symptoms of decline stood out like beacons, more firms would recover in time. But symptoms have to be looked for and there is usually no time left if one would wait for the beacon or signals to light up. (

Sickness does not set in overnight; it is a gradual process with distinct stages. (7) An entrepreneur of a sick unit can get various signals, or symptoms of sickness, as under. The following list is not exhaustive, but illustrative.

1. **Shortage of Capital**
   One symptom of sickness is shortage of working capital. A firm will experience this and it would require additional overdrafts from its banker frequently. It is true that shortage of working capital would not necessarily mean sickness, as such shortage may be on account of inadequate credit facilities given by the banker. But then it should be remembered that inadequate bank finance itself can also cause sickness. Many times...

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an entrepreneur will find it difficult to pay instalments of term loans to the banks/institutions. This will be a chronic feature.

(2) Under-utilisation of Capacity
This is also one of the symptoms of sickness. It is really surprising that T.Tiwari Committee has stated under-utilisation of capacity as one of the causes of sickness instead of quoting it as a symptom of sickness.

(3) Declining sales or reduction in market share

(4) Balance sheet signals like low profitability, current ratio debt equity ratios, decline in net worth, low return on investment etc.

(5) Excess Inventories.

(6) Non-financial symptoms like strike or labour trouble, high turnover of employees, frequent break down of plant and machinery etc.

(7) Delays in the implementation of a new project.
Symptoms of sickness, that can be seen by the bank

The projects or units do not become sick all of a sudden but many a time, it is a result of delays and cost overruns during the implementation stage. Delayed availment of financial assistance itself does indicate overrun in the project cost, but this aspect is often not noticed by banks or financial institutions.

It is said that the signals or symptoms of sickness are literally dropped at the banker's doorstep, and a careful and regular study of the transactions recorded in the cash credit account of the borrower can reveal vital aspects. A banker should become alert if he observes features in the accounts like persistent irregularity in the accounts, frequent requests for overdrawings, chronic non-payment of loan instalments, frequent return of cheques, unsatisfactory turnover in the account as compared to sales. If the number and amount of bills submitted are decreasing and sanctioned bill limit is not being fully utilised, it may indicate that sales have come down and that the unit may be tending towards sickness.

Another important source of signal for the bank is the monthly stock statement. Gradual accumulation of unsold finished goods may either indicate a low demand in the market or a tendency to earn a trading profit through hoarding.
A banker can get various warning signals from financial statements by analysing various items such as trend of sales, capital base or net worth of the firm indicating owner's stake in the business, debt-equity relationship, position of trade debtors vis-a-vis sales, availability of net working capital (i.e. excess of current assets over current liabilities), position of inventory, profitability of the firm etc.

Apart from making relatively simple and traditional analysis of financial statements, certain authors like Altman, Miller, Beaver, and L.C.Gupta have tried to develop certain models for predicting failure or sickness with the help of ratio analysis. Miller attempted in 1966 a cause and-effect ratio approach and divided ratios into two categories - (i) causal ratios, and (ii) ratios that measure effect. There was however criticism against Miller's approach that his analysis seeks merely to trace a cause-and-effect relationship among ratios and not between a ratio and the ultimate survival of a firm. (B) Prof. Altman of New York University developed a model for predicting corporate failures based on a statistical procedure known as 'multiple discriminant analysis' (MDA). The multiple discriminant analysis (MDA) is a statistical technique borrowed

by him from the biological and anthropological sciences in which researchers may ask the following type of question — to which of the two or more a priori population — groups (male or female, Mongol or non-Mongol, etc.) does a particular item belong? The classification is achieved by measuring the various quantifiable characteristics of the item. MDA attempts to derive linear (or quadratic) combinations of these characteristics which 'best' discriminate between the specified populations. The analysis is, in a sense analogous to multiple regression analysis, except that whereas the dependent variable in regression analysis takes on continuous values, the dependent variable in MDA represents different groups or categories. Prof. Altman, by using multiple discriminant analysis, showed a way of combining several financial ratios into a single index Z. Altman used the following five ratios —

i) Working Capital / Total Assets (X_1)
ii) Retained earnings since inception / total assets (X_2)
iii) Earnings before taxes and interest / Total assets (X_3)
iv) Market value of Equity / Book value of Total debt and (X_4)
v) Sales / Total assets. (X_5)

The discriminant function derived by Altman was as follows:

\[ Z = 0.012 X_1 + 0.014 X_2 + 0.033 X_3 + 0.006 X_4 + 0.999 X_5 \]

X refers to the five financial ratios listed above and Z is the overall index. A cut-off point for the 'Z' score is determined.
in such a way as to minimise the overlap between bankrupt and non-bankrupt groups. The Z score is calculated for each company which forms the basis of classification for the company as either bankrupt or non-bankrupt. The cut-off point is set in relation to past prediction accuracy. It was computed by Altman that a sick company had a score less than the cut-off point (2.6) while a healthy company scored more than this. (9) It means that if a company has 'Z' score more than 2.6, then it is a healthy unit and if 'Z' score is less than 2.6, then the unit may be a sick unit. (10) The one year prediction for which Altman claims an accuracy of 95 percent will in practice, no prediction, comments Dr. Gupta, an Indian Researcher, because financial statements used to predict bankruptcy one year ahead would reach the analyst’s hands in most cases only after the bankruptcy petition has already been filed. (11)

Dr. Gupta (an Indian Researcher) is attracted by Beaver's study which included 30 different financial ratios and their relative efficiency to predict failures up to five years, prior to failure. Dr. Gupta has mentioned that the balance sheet ratios are better indicators of the 'reserve strength' of an enterprise and among them, solvency ratios are more

reliable than liquidity ratios. After all, finance follows where enterprise leads. He has further mentioned that empirical results point out the existence of a definite association between the incidence of sickness and inadequacy of equity base, implying that companies with inadequate equity base have little 'reserve strength'.

Dr. Gupta has employed 25 profitability and 31 balance sheet ratios and has concluded about the superiority of profitability ratios as early warning signals of sickness.

I am however doubtful about practical utility of Dr. Gupta's work, in predicting sickness, particularly in the case of small scale industries, keeping in mind the difficulties faced by a banker in receiving financial statements and other necessary information to look into inter-firm comparison. Besides, a banker may not have the time to spend on such an analysis. It is also likely that a company which is going to bust or fail may distort its published accounts or financial statements. The technique of skillfully distorting financial statements is described as 'creative accounting' by John Argenti and he has given a list of about 18 accounting techniques which make company's results look better than they really are.

P.V. Satyanarayana (13) expressed that Altman's model may not be useful in India for predicting corporate collapse, because in India despite continuous cash losses companies do not close down as in case of UK or USA.

Dr. Kaveri (of NIBM) has observed that amongst different ratios, five ratios are more significant, particularly for predicting health of borrowing firms, especially the small scale sector. (14) These ratios are -

(a) Current ratio
(b) Stocks / Cost of Goods sold
(c) Current Assets / Net Sales
(d) Net Profit (before tax) / Total Capital Employed
(e) Net Worth / Total outside liabilities.

I have calculated all these five ratios in respect of 66 units surveyed by me, wherever I could get financial statements from the entrepreneurs. However, instead of computing the ratio Net Profit (before tax) / Total Capital Employed I calculated the ratio of Net Profit (before tax)/ Sales, due to superiority of profit to sales ratio over profit to - asset/total capital employed ratio.


The reason for superiority of profit to sales ratio is that the distorting effect of price-level changes on inter-firm comparison of profitability is quite serious when book value of assets is used as denominator in the ratio, while sales values are largely free from such distortion. These ratios have been given in Annexure A (Table No.29). It was observed that these ratios were adverse or deteriorating almost in all the cases of sick units, as compared to healthy units. But even in the case of certain healthy units, some of these ratios, more particularly current ratios and Total outside liabilities to net worth ratio, were adverse. Although usefulness of these ratios in predicting health of a borrowal unit (particularly SSI unit) cannot be ruled out completely; I feel that its use is quite limited.

Apart from various financial signals received by the banker mentioned above, a banker also gets certain non-financial signals such as strike/lockout in the factory, high labour turnover, break down of plant and machinery, death of a key partner/director etc. If a banker or even an entrepreneur himself would be vigilant and keep a watch on the performance of the unit and would also know the health of the unit through various signals mentioned above.

ne (i.e. either banker or entrepreneur) can prevent sickness by suggesting/taking corrective measures, at the right time. Once danger signals are thrown up in case of a borrower and signs of difficulty emerge, speedy action is called for on part of the banker and timely and firm handling are of essence. (16) In such cases, a banker may intervene even in management, if that is necessary, in the interest of all concerned. It was also observed by the Tandon Committee that in such cases, a major inhibiting factor has been the reluctance of the banker to offer advice to industry on what steps to take to restore health or intervene to improve management in specific areas of deficiency, or even to remove undesirable practices. (17)

**Causes of Sickness or Failure**

Causes of sickness are innumerable. Different factors contribute to sickness of industrial units, either singly or in conjunction with other factors. The causes of sickness can be broadly classified into two groups - (i) internal causes and (ii) external causes. However before we see the specific internal and external causes of sickness, let me make a mention of factors or situations which make units sick during the course of implementation of projects.

(16) Reserve Bank of India "Report of the Study Group to Frame Guidelines for Follow up of Bank Credit" (Tandon Committee) (RBI) 1975, Page 59.
(17) Ibid - Page 59.
Difficulties in the course of implementation of projects:

Infant mortality is more common in industrial enterprises. Brough's study of 100 failed companies showed that a quarter of them were wound up within two years and 62 were wound up in less than five years. (18) William A. Delaney has mentioned that in USA 95 percent of the small ventures do not survive for eight to ten years, and that 50 percent of newly started units are closed, within a period of one year. (19)

One of the most outstanding feature of failure statistics is the high propensity on the part of young firms to fail. The longer a company survives, generally, other things being equal, the smaller becomes the probability of failure. (20)

It was observed by the Indian Institute of Economics that more than 40 percent of the units in each of the states of Andhra Pradesh, Kerala and Karnataka do not have life span of more than two years and that 25 percent of the units died in the second year and another 20 percent in the third year. The symptoms indicated that infant mortality is on account of delay in implementation of the project and over-run in its cost.

(18) Lal Sudarshan "How to Prevent Industrial Sickness" (Navrang, New Delhi) 1978, Page 9. (It is not mentioned in which year this study was conducted).


A project report envisages completion of certain activities, incurring costs within a stipulated time schedule for starting production and sales at a desired time. Except for very small projects, in the present Indian context, it is not always possible and probably impossible for promoters to start production and sales at the desired level at the time envisaged in the project document. Time and cost overrun are interrelated. Unfortunately, in India, overrun is the rule and not the exception. (22) Pickup any newspaper, any day, and you are likely to find at least one project in the news for this reason. It was observed that delays and cost overruns are crucial factors responsible for rendering several projects sick. (23) The famous physicist, Einstein once said "cost is supposed to be based on facts but - the facts are wrong!" O.P. Kharbanda and E.A. Stallworthy suggested to take some time to make a sound assessment of project cost and duration, before starting. There will be fewer overruns in cost and time if the estimates are better. In the U.S.A. the art and science of the cost control of projects are well developed and well understood. There are networks, such as CPM (Critical Path Method) PERT (Programme Evaluation and Review Technique), precedence, and a host of others, which are being used for time and cost controls of

(22) Kharbanda O.P. and Stallworthy E.A. "How to Learn from Project Disasters" (Gower Publishing Co. Ltd. UK) 1983, Page 37.

(23) Western Regional Seminar on causes and incidence of Sickness among small enterprises assisted by State Level institutions and banks, held on 20th & 22nd April 1979.
projects. However, even then projects are getting delayed due to practical difficulties.

There are certain most unexpected internal as well as external factors involved in any project over which the entrepreneurs have absolutely no control. In such cases higher costs over estimates and delays in completion appear inevitable and therefore have to be accepted. But there are many elements which can be controlled and costs can be kept within limits and projects can be completed in reasonable time.

When a project is in the stage of formulation, there is a tendency to underestimate its capital cost. The underestimation is motivated by the desire to reduce promoter's contribution. Similar was the finding of a Seminar held at Bangalore, (24) and it was observed that some entrepreneurs deliberately underestimate the cost of the project so as to classify themselves as small scale unit, to enable them to avail of concessions available, as also to keep their own contribution to the minimum. In the course of implementation however, the project cost increases and the promoter with his constraint in resources has to go to financial institutions.

(24) Southern Regional Seminar on causes and incidence of sickness among small entrepreneurs, organised by Development Banking Centre (DBC) of Management Development Institute, New Delhi. (1979)
for further finance or resort to private borrowings at exhorbitant interest rates. This results in higher cost of the project and further delay in its implementation.

There is need for a realistic assessment of provision for contingencies particularly in the context of galloping inflation. Similarly, it is necessary to make provision for interest on term loans, during the construction period, in the project cost. The importance of making these two provisions will be realised after going through the case study of a unit manufacturing gauges. (Please refer Chapter IX on case studies).

While working as an Officer in the advances department of a bank I have observed that many a time, entrepreneurs do not fill in the details of time schedule of implementation of project, in their loan applications and when this information is specifically asked by the banker, the approach of the entrepreneur is casual and he does not give a serious thought to such important aspect of the project report. For the purpose of preparation of project report, many entrepreneurs are dependent on outside consultants, who do not pay adequate attention to these aspects, perhaps not realising its importance. Similar is the case of sales forecasting on which the entire cash flow is dependent. Many times, entrepreneurs do not realise the importance of preparing projected cash flow statements based on realistic sales estimates. Some
entrepreneurs, as it appears from their approach, prepare the project report just to complete bank formalities to enable them to get credit facilities sanctioned from banks/term lending institutions. The banks/financial institutions, who should make a thorough appraisal of such project reports often have their own limitations of time and trained officers. Some times when a banker is doing a detailed appraisal of a project, his calling of additional information/queries, is taken by the entrepreneurs as 'bank's tactics', prompting him to make complaints against the banker. Jeffry A. Timmons has rightly observed that the business plan or project report is taken by an entrepreneur essentially as a negotiating and selling tool for raising money. It is not considered relevant and useful beyond that.\(^{(25)}\)

I have already mentioned in Chapter No.VIII on "Problems of Small Scale Industries" and in earlier Chapter No.VII on General information about Selected Units that as the sample units selected by me were more than 15-20 years old, I could not get copies of project reports prepared by them at the time of starting the unit and compare the projections of cost of project, sales, profit etc. with the actuals. However, entrepreneurs of many selected units informed me that they did not face any difficulty during implementation stage of the project though in certain cases they had some difficulties.

\(^{(25)}\) Timmons Jeffry A. "A business plan is more than a financing device" Harvard Business Review, March-April 1980. \hspace{1cm} .241.
In a few cases although the entrepreneurs informed me that there was overrun in project cost, it was marginal and did not affect viability of the project. I have however given two case studies in the Chapter on Case Studies from which difficulties faced by entrepreneurs during implementation stage can be observed. However in respect of case study on unit manufacturing 'filter pads' the unit did not become sick, despite wrong project planning, due to its excellent performance on sales side and banker's helping hand in difficult situations, some times even by ignoring the usual credit norms. As regards another case study of a unit manufacturing 'gauges', the unit became sick due to escalation in project cost and inaccurate forecast of demand for the company's products.

I have therefore formed an opinion that a unit can become sick due to faulty project planning and cost and time overruns, if it fails on the marketing side also. If overrun is substantial and profit margin is low either due to low sales turnover or lower profitability, then the unit can become sick despite its achieving sales as per project report. I therefore feel that project reports should be prepared with utmost care and adequate provisions should be made in project cost, towards contingencies and interest on term loans during construction period. Needless to add that a banker should also make a detailed and critical appraisal of projects.
John Argenti (26) has suggested to make sensitivity analysis, by altering each major assumption like costs, revenues, time-schedules etc. which will improve project appraisal by banks. It was the view expressed by representatives (27) of banks & financial institutions to T. Tiwari Committee that implementation of a project should also be closely monitored by the banks and financial institutions to regulate the expenditure as per the schedule, so as to avoid any large cost overrun and time overrun.

Causes of sickness in case of existing units or units under regular production:

The causes of sickness in the case of existing units or units under regular production can be classified into four broad areas - viz. (i) production area (ii) marketing area (iii) management area and (iv) the finance area. Besides, in the case of each area sickness might have been caused due to internal factors or external factors. I am giving below some important causes of sickness in these four broad areas.

(27) Reserve Bank of India "Report of the Committee to examine the legal and other difficulties faced by banks and financial institutions in Rehabilitation of Sick Industrial Undertakings and suggest remedial measures including changes in the Law" (R.B.I.) 1984, Page 39.
(1) Production Area

(A) Internal causes

i) Machinery break down on account of lack of maintenance and deferment of essential replacement.

ii) Poor quality of raw material chosen.

iii) Low technical competence, or inadequate technical know-how.

iv) High material wastage.

v) Lack of production planning and control.

vi) Unbalanced machinery set up.

vii) High inventory and lack of inventory control.

viii) Lack of skilled labour and proper supervision.

ix) Deteriorating labour relations.

x) Deterioration in quality of finished products leading to high rejections.

xi) Lack of timely and adequate modernisation.

(B) External causes

These are the factors which are generally beyond the control of management of the unit, namely -

i) Poor quality of raw material.

ii) Power shortage.

iii) Shortage of raw material.
iv) Political uncertainty affecting industrial relations and loss of manhours.

v) Inter-union rivalry.

vi) Change in government policy affecting import of raw material.

vii) Inadequate bank finance for modernisation of plant and machinery.

(II) Marketing Area

(A) Internal causes

i) Dependence on one or a few buyers.

ii) No proper study of market.

iii) Poor marketing effort.

iv) No proper distribution channels or weak market organisation.

v) Large order book without escalation clause in the inflationary market conditions.

vi) Problem of product-mix due to lack of orders or capacity.

vii) Lack of market feedback and market research.

(B) External

i) Recession in the industry.

ii) Severe competition (more units chasing limited market). Some times, this factor can be classified
under 'internal' reasons, because the entrepreneur has failed in doing proper market study, due to which he could not get a clear idea about market conditions.

iii) Faster obsolescence of product than expected, due to technological developments, e.g. liberalisation of import policy in respect of computers of high technology (and latest models) may lead to sickness in indigenous computer manufacturing units.

iv) Decline in Government investment affecting the product line of the unit.

v) Rise in the cost of production unmatched by a commensurate rise in sale price of end product particularly when the product is under price-control.

(III) Management Area

(A) Internal causes

i) One man rule and lack of proper organisation.

ii) Lack of planning and control.

iii) Un-planned diversification or lack of diversification.

iv) Dishonesty.

v) Dissent among partners / working directors.

vi) Poor record keeping.
vii) Insufficient experience and education of entrepreneurs.

viii) Lack of professionalism and control.

(B) External causes

i) Death or ill-health of a key partner/director.

ii) Non-availability of managers for small-scale industries.

(IV) Finance Area

(A) Internal causes

i) Weak equity base - high debt gearing.

ii) Poor collection efforts and high receivables.

iii) Unplanned expansion.

iv) Over trading.

v) Diversion of funds for expansion of business or private investment.

(B) External causes

i) Inadequate finance by bank and/stiff repayment schedules - delayed decisions.

ii) General credit restriction affecting liquidity of a unit particularly in its expansion phase.

iii) Delayed payments by clients, inspite of proper collection efforts.
Apart from the above causes there could be some other reasons for sickness like -

i) Floods or other natural calamities.
ii) Bottlenecks in transport facilities.
iii) Locational problems.
iv) Government policy in respect of various matters.
v) Political situation (domestic as well as international).

In the previous paragraphs, I have tried to give some of the important symptoms and causes of sickness of SSI units which were based on my own experience as a credit officer, opinions of certain industrialists, heads of financial institutions, and management institutions and various articles appeared in Journals / news papers etc. and Tiwari Committee Report (1984) (Pages 21 to 23). I would now give findings of some other committees and/researchers in respect of causes of sickness.

The United States Department of Commerce made a study of 487 business establishments which went into bankruptcy in New Jersey. It was observed that out of the total number of businesses studied 23.5 per cent kept no books, 29.4 per cent kept inadequate books and 39 per cent never took
an inventory. Although many of those who failed blamed business depression, an analysis of the data indicated that business depression was the occasion rather than the causes of failure, and that inefficient management was the real cause.\(^{(20)}\) According to Slatter\(^{(29)}\) there are 11 principal causes of decline of a firm. They are lack of financial control, inadequate management, competition, high cost structure relative to competition, changes in market demand, adverse movements in commodity markets, acquisitions, financial policy, overtrading etc.

The following figures give an account of business failures in England & Wales.\(^{(30)}\)

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\(^{(20)}\) Kelley Pearce C. & Lawyer Kenneth - "How to Organise and Operate a Small Business" (Prentice Hall Inc.) 1949, Page 80-81.


(The percentage of failure not mentioned).
It will be observed from the above figures that business failures have nearly doubled from 6890 in 1980 to 12,067 in 1982, just in 3 years. Reasons for such failures are basically the failures of management to predict a crisis situation usually accompanied by a stagnant business and a continuous decline of profits for at least 3-4 years.

A study of 378 large units by the Reserve Bank of India in December 1979 revealed that the following factors were responsible for sickness.

<table>
<thead>
<tr>
<th>Causes of Sickness</th>
<th>No. of Units</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>1) Mismanagement</td>
<td>197</td>
<td>52</td>
</tr>
<tr>
<td>2) Faulty planning and technical drawbacks.</td>
<td>52</td>
<td>14</td>
</tr>
<tr>
<td>3) Market demand/recession</td>
<td>86</td>
<td>23</td>
</tr>
<tr>
<td>4) Labour troubles</td>
<td>9</td>
<td>2</td>
</tr>
<tr>
<td>5) Other reasons like power cut, shortage of raw materials.</td>
<td>34</td>
<td>9</td>
</tr>
<tr>
<td>Total:</td>
<td>378</td>
<td>100</td>
</tr>
</tbody>
</table>
The report of the Study Team of the State Bank of India (1975), headed by Shri J.S. Varshneya, which made a study of 120 SSI units, observed that following features appeared frequently in the unsatisfactory units.

(a) A large number of units studied lacked management expertise. This was evident from the fact that there was no planned approach to the various activities in key areas like finance, marketing etc. Virtually all units suffered from lack of suitable organisation and a proper Management Information System.

(b) Most of the units had a poor equity base, which gave rise to the initial problems, leading to a chain of adverse situations.

(c) Established units, which had been doing well for long periods did not appear to build up any internal financial strength to provide for contingencies.

(d) Once a unit is in trouble, it gets into a vicious circle, from which it is not able to come out.

According to another survey of SSI Units in South India (31) lack of finance is one of the major causes of mortality and as a cause of mortality this reason operates alone or in combination with other major causes like shortage of raw material and inefficiency in management.

The team which surveyed 50 sick small scale units in 1975 in Vidarbha made a few general observations as under:

"That most of the difficulties of small scale units arise from financial and administrative rigmarole; that spiralling interest charges and demand recession tend to make units sick; and that requirements of credit of small scale units located at a far away place would be higher than those located at an industrial centre because they have to maintain higher inventories, and that institutional financial agencies have failed in acting as sentinels of progress, growth, employment etc."

A.C. Hazel and R.S. Reid in their book "Managing the Survival of Smaller Companies" (1973) have divided causes of failure into three parts as under.

(a) "It can happen to you - But entrepreneur should not blame himself" - Examples of causes are - catastrophes and disasters, inflation and world events, economic and government changes, localised depressions, death and domestic crisis, etc.

(b) "Perhaps it could be partly your (i.e. entrepreneur's) fault" - Examples of causes are -
bad debt losses, large-scale competition, low profit margins, shortage of key raw materials, fraud, machinery break down etc.

(c) "No one can be blamed, but entrepreneur himself" -
Examples are - market domination, too little diversification, changing markets and materials, using too few suppliers, reliance on too few customers, market saturation, excessive credit and bad debts, adverse personal factors, excessive overheads etc.

Prof. Altman has mentioned in his book Corporate Bankruptcy in America that if one is looking for a way to predict failure, it is not enough just to look at the firm itself, at its management, accounting ratios and so on. All these are important, but never forget that there are powerful external forces acting from outside the firm as well, like GNP (Gross National Product) money supply and stock market performance. Findings indicated that a firm's propensity to fail is heightened during periods of reduced economic growth, stock market performance and money supply conditions. (33)

The Committee appointed under the Chairmanship of T. Tiwari collected information on the causes of 341 sick industrial units (during the period 1981 to 1983) from various banks/financial institutions. The committee observed that management deficiency (which also includes dissensions in management, mismanagement, weak management and dishonest management) is the most widespread cause of industrial sickness, found in almost two-thirds of the 341 sick industrial units studied. (34) The details of causes of sickness of 341 units are given in Table No. 30 in the Annexure A.

The Study Group appointed under the Chairmanship of Dr. P.D. Ojha analysed factors responsible for success or failure of nursing programmes, in 56 cases relating to banks and SFCs (33 successful and 23 unsuccessful). It was observed that the major factors responsible for the success of nursing programmes in these cases were provision of adequate finance, better management and improvement in market conditions. (35) The major factors which assisted or

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(34) Reserve Bank of India "Report of the Committee to examine the Legal and other difficulties faced by banks and financial institutions in Rehabilitation of Sick Industrial Undertakings and suggest Remedial Measures including changes in the Law" 1984, Page 27.

(35) Reserve Bank of India "Report of the Study Group to examine the issues relating to the setting up of Soft Loan Assistance Fund for Rehabilitation of sick small scale industrial units" (RBI) 1985, Page 19.

---
operated against the successful implementation of nursing programmes, (in the opinion of the concerned institutions) in these 56 cases have been tabulated and given in the Annexure A (Table No.31). It may be interesting to note from Table No.31 (given in the Annexure) that a single major factor responsible for success or failure of the nursing programmes was the quality of management.

Mr. Amio Kumar P.C.Ghosh (35) has mentioned in his Ph.D. thesis that apart from non availability of bank credit the major problems confronting the units were capacity under-utilisation, power failure, restrictions on power consumption, inadequacy of orders, seasonal demand, lack of demand for new products, absence of quality control leading to limited competitive capacity. He has further observed that inadequacy of finance was only one of the problems and it was not created by bankers' frequent denial to accommodate the units, but by delayed payments made by the big units, which were the customers of the small units.

As regards the survey taken by me, I have already mentioned that 15 units, out of 66 units or 22.72 per cent of the units were found to be sick. On next page in Table X-A, I have given the causes of sickness of these 15 units.

## TABLE - X-A

Causes of Sickness of Selected Units.

<table>
<thead>
<tr>
<th>Industry</th>
<th>No. of Units</th>
<th>Finance (1)</th>
<th>Marketing (2)</th>
<th>Labour (3)</th>
<th>Production (4)</th>
<th>Management (5)</th>
<th>(2)*(3)</th>
<th>(2)*(4)</th>
<th>(2)+(5)</th>
<th>(2)+(1)</th>
<th>(5)+(1)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Light Engineering</td>
<td>6</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>3</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>Basic Metal &amp; Metal Products</td>
<td>3</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Chemicals &amp; Chemical Products</td>
<td>4</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>2</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Paper &amp; Paper Products</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Miscellaneous</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>15</strong></td>
<td><strong>1</strong></td>
<td><strong>3</strong></td>
<td><strong>1</strong></td>
<td><strong>3</strong></td>
<td><strong>3</strong></td>
<td><strong>2</strong></td>
<td><strong>1</strong></td>
<td><strong>1</strong></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
It will be observed from the above Table (Table X-A) that out of 15 sick units, 12 units or 80 per cent of the units have become sick either due to single reason of marketing problem or due to combination of problem of marketing with some other problem in areas like finance, management, labour, production etc. It was observed that where a unit has become sick due to combination of some other cause, along with marketing, the most dominant reason remained marketing problem. In the case of units facing problem of marketing, it was observed that in many cases entrepreneurs were aware of the real cause of sickness, but were helpless as the situation was worse and beyond their control and there were no hopes of any recovery. In one case, when the entrepreneur could notice recessionary tendencies in the market, coupled with labour trouble, he immediately closed the unit by making payment to labour and also to the banker. However other entrepreneurs could not take such steps, as they could not judge the situation so quickly as in the case of this unit.

Surprisingly, as against the common criticism that units are becoming sick due to financial problems, (Please refer Survey Report of Committee on Sick Units in Vidarbha, survey of mortality of SSI units in South India etc.) it was observed that in the case of only one unit, the unit had become sick due to problem in the area of finance. In
this case, however, as it appeared, the unit has become sick due to the banker's mistake in not providing adequate financial assistance at the right time. I have discussed the case of this unit separately in Chapter No.IX on Case Studies (Case study No.4).

I had asked various questions to entrepreneurs of sick units such as (i) when were the losses detected/noticed by entrepreneur? (ii) what efforts were made by entrepreneur to minimise losses and whether efforts were successful? (iii) whether unit was facing working capital shortage? (iv) Reasons of working capital shortage (v) whether banker was approached for assistance? The replies given by entrepreneurs have been tabulated and are given on next page.
It will be observed from the above Table (Table X-A) that out of 15 sick units, 12 units or 80 per cent of the units have become sick either due to single reason of marketing problem or due to combination of problem of marketing with some other problem in areas like finance, management, labour, production etc. It was observed that where a unit has become sick due to combination of some other cause, along with marketing, the most dominant reason remained marketing problem. In the case of units facing problem of marketing it was observed that in many cases entrepreneurs were aware of the real cause of sickness, but were helpless as the situation was worse and beyond their control and there were no hopes of any recovery. In one case, when the entrepreneur could notice recessionary tendencies in the market, coupled with labour trouble, he immediately closed the unit by making payment to labour and also to the banker. However other entrepreneurs could not take such steps, as they could not judge the situation so quickly as in the case of this unit.

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<table>
<thead>
<tr>
<th>Industry</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
<th>6</th>
<th>7</th>
<th>8</th>
<th>9</th>
</tr>
</thead>
<tbody>
<tr>
<td>Engineering:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1) Unit - A</td>
<td>1st month</td>
<td>Closure of unit</td>
<td>Yes</td>
<td>-</td>
<td>No.</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2) Unit - E</td>
<td>3rd month</td>
<td>Cost reduction and improvement in labour relations</td>
<td>No.</td>
<td>Things</td>
<td>Yes.</td>
<td>No.</td>
<td>Beyond bank's normal norms.</td>
<td>Low sales turnover due to strike.</td>
<td></td>
</tr>
<tr>
<td>3) Unit - C</td>
<td>3rd month</td>
<td>Increase sales with the help of additional bank finance</td>
<td>No.</td>
<td>Recession</td>
<td>Yes.</td>
<td>Yes.</td>
<td>-</td>
<td>Low sales turnover.</td>
<td></td>
</tr>
<tr>
<td>4) Unit - D</td>
<td>3rd month</td>
<td>Increase sales with the help of bank finance</td>
<td>No.</td>
<td>Things</td>
<td>Yes.</td>
<td>No.</td>
<td>As per bankers assistance was sufficient.</td>
<td>Low sales turnover.</td>
<td></td>
</tr>
</tbody>
</table>
Table X-B (contd...)

<table>
<thead>
<tr>
<th></th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
<th>6</th>
<th>7</th>
<th>8</th>
</tr>
</thead>
<tbody>
<tr>
<td>6</td>
<td>Unit - F</td>
<td>1st month</td>
<td>Cost reduction</td>
<td>No. Things were beyond control</td>
<td>Yes.</td>
<td>No. Approach of bank officials</td>
<td>Low sales due to inadequate bank finance</td>
<td></td>
</tr>
<tr>
<td>7</td>
<td>Basic Metal</td>
<td>3rd month</td>
<td>Diversification on product line</td>
<td>No. 1. Major client had stopped sales order.</td>
<td>Yes.</td>
<td>Not sought</td>
<td>Low sales turnover</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>2. Diversification was not timely.</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>8</td>
<td>Unit - H</td>
<td>3rd month</td>
<td>Cost reduction</td>
<td>No. Things were beyond our control.</td>
<td>Yes.</td>
<td>No.</td>
<td>Low sales turnover</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Diversion of funds by us to other activity.</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>1. Diversion of funds</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>2. Low sales turnover</td>
<td></td>
<td></td>
</tr>
<tr>
<td>9</td>
<td>Chemicals</td>
<td>After two years</td>
<td>Increase sales</td>
<td>No. Market saturation and competition</td>
<td>Yes.</td>
<td>Yes</td>
<td>Low sales turnover</td>
<td></td>
</tr>
<tr>
<td>10</td>
<td>Unit - J</td>
<td>No proper replies given as entrepreneur was not ready to admit that the unit has almost become sick.</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>11</td>
<td>Unit - K</td>
<td>No proper replies given as entrepreneur was not ready to admit that the unit has almost become sick.</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>1.</td>
<td>2.</td>
<td>3.</td>
<td>4.</td>
<td>5.</td>
<td>6.</td>
<td>7.</td>
<td>8.</td>
</tr>
<tr>
<td>---</td>
<td>---</td>
<td>---</td>
<td>---</td>
<td>---</td>
<td>---</td>
<td>---</td>
<td>---</td>
<td>---</td>
</tr>
<tr>
<td>12) Unit - L</td>
<td>3rd month</td>
<td>No efforts were made as losses were due to external factor beyond our control.</td>
<td>Yes.</td>
<td>No. Credit limit</td>
<td>1. Delayed adequate in payments. banker's opinion.</td>
<td>2. Low sales.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>13) Unit - M</td>
<td>No proper replies were given. Sickness due to low sales, but unit is blaming banker.</td>
<td>Sales - Rs. 0.90 lakh</td>
<td>Bank Finance: Working Capital Rs. 4.30 lakh</td>
<td>Term Loan Rs. 11.30 lakh</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

*Note:* It was not possible to interview and obtain replies on the above points from 2 entrepreneurs of sick units.
It will be observed from Table X-B that in the case of almost all units excepting 2 units, the entrepreneurs were able to detect that their unit was incurring losses within 3 month's time. However in the case of two units it took almost a year's time or even more for the entrepreneur to know that the unit was incurring losses.

As regards units J and K, no proper replies were given by the entrepreneurs, as they did not accept that their units have become sick. I however came to know that these units are sick units, after studying their balance sheets, which showed cash losses for the last one or two years and from the other replies of entrepreneurs from which it was observed that there is no improvement in the situation for the current year also. In one case, it appeared that the entrepreneur was perhaps not ready to accept the signals of sickness, which appeared from balance sheet of his company. In this case, as it has been pointed out by A.C.Hazel and A.S.Reid\(^{(37)}\) that entrepreneurs do not want to know bad news, with the result that, like a wronged husband or wife, entrepreneurs are the last to see something that others have suspected for ages.

But in case of unit K, where balance sheet of the firm showed continuous cash losses for 3 years, the managing

\(^{(37)}\) Hazel A.C. & Reid A.S. - "Managing the survival of smaller companies" (Business Books Ltd.) 1977, Page 7.
partner skillfully avoided to answer the questions raised by me about detection of losses and efforts made etc. The managing partner even did not look worried about continuous cash losses. This naturally created doubts in my mind about reliability of balance sheet figures. As I made analysis of balance sheet I observed that the unit was maintaining stocks as under -

<table>
<thead>
<tr>
<th></th>
<th>1980</th>
<th>1981</th>
<th>1982</th>
</tr>
</thead>
<tbody>
<tr>
<td>Stocks</td>
<td>99.38</td>
<td>102.39</td>
<td>93.04</td>
</tr>
<tr>
<td>Sales</td>
<td>159.70</td>
<td>142.59</td>
<td>148.16</td>
</tr>
</tbody>
</table>

(Rs. in lakhs)

It was also observed by me that a major portion of stocks comprised of stock of imported raw materials. I therefore suspect that the unit is purposely hoarding higher stocks of material, for the purpose of taking advantage of favourable market situation at a later stage. Besides, the losses shown in the balance sheet were not real losses, and the firm was showing losses mainly to avoid payment of income-tax and to take advantage of the benefits available to sick units. Such doubts were further strengthened when it was observed that all partners were in wholesale trading business since long. (In fact it was and is still a family business). However such doubts/conclusions are subjective in nature and are difficult to prove objectively. I have therefore considered this unit also a sick unit.
It will be observed from Table X-B that out of 11 units (i.e. sick units where I had received replies to my questions) entrepreneurs of 10 units (or 90 percent of sick units) expressed that they were facing shortage of working capital. But out of these 10 units, only in one case, banker was found to be partly responsible for shortage of working capital which ultimately led to low sales turnover and sickness of the unit. But in all other cases the low sales turnover led to shortage of working capital and in such cases the entrepreneur expected that the banker should go out of his way to extend additional credit facilities.

It was observed that in case of units where there was some possibility of increasing sales turnover, the banker sanctioned credit facilities, which was also not of much help for improving health of the unit due to units' inability to increase sales on account of various reasons like market recession, competition, market saturation, managerial inefficiency etc. On the contrary additional credit facilities increased interest burden of the unit, thereby increased the level of break-even sales. In fact the observation of A.M. Woodruff & T.G. Alexander (38) that the unsuccessful companies did not suffer from a shortage of working capital until their financial collapse was critically near, proved to be very much true.

Similarly, William A. Delaney has mentioned in his book (39) that a problem like low sales or rising costs or delayed payments of accounts receivables cause a small businessman run out of money. But, instead of solving this problem the small businessman goes to a banker for additional credit facilities. Thus asking for loan or additional credit facilities is treating the effect, and not the cause of one's problem. In such situation if the banker grants loan to tide over the difficulty, with no questions asked, then in all likelihood, an entrepreneur will return to banker a few months later with the same problem and in a worse situation, without repaying old loan. This happens because the real cause of negative cash-flow has not been treated.

Besides Dr. S.D. Kopardekar, who made a study of some selected small scale units from Pune in the year 1969-70 observed that although most of the small entrepreneurs tended to interpret all their difficulties in terms of shortage of capital, a close analysis showed that the real reason was organisational one. (40) It was observed in Gujarat that even when 100 % finance was provided to new enterprises,

(40) Kopardekar Dr. S.L. "Small Scale Industries - A Study in Investment and Output aspects" (G.Y.Rane Prakshshan) 1974, Page 314.
the success of a small enterprise depends upon the entrepreneurial and managerial competence of the man behind the project and soundness of his proposal. (41) All this evidence suggests that my hypothesis No.1 that "shortage of working capital is generally not the major cause of sickness but is symptomatic of some other inadequacies like marketing" is true.

It was observed by me that very few entrepreneurs planned for financial emergencies, and that whenever such financial emergencies occurred the entrepreneurs relied and called upon only one source i.e. banks. When I asked a question to entrepreneurs as to what efforts were made by them to minimise losses, many entrepreneurs replied that they tried to increase sales turnover by availing additional bank finance. Some entrepreneurs said that they tried to control costs and reduce losses. But no entrepreneur replied that he first utilised his reserves, which were kept by him for such financial emergencies. Such reserve funds could have been created by way of utilising unutilised overdraft limits or by selling excess stocks, or by trying to realise debts quickly or trying to liquidate a part of unimportant assets etc. One should remember that it is easiest to get maximum credit facilities sanctioned when times are good.

(41) Hutchinson P.J. (Editor) "Financing Small Enterprise Development" (Financial Management Research Centre, N.S.W.) 1981. - Article by V.G.Patel, Page 207.
In fact, I have observed that many successful large companies are keeping a large portion of their working capital limits unutilised and they draw these limits to full extent in case of financial crisis. But very few small scale units have followed this policy. Moreover, most of the small scale firms do not appear to have any financial planning and they try to manage the things on day to day basis. On the contrary, there are many instances where short term funds are diverted for long term uses, within the same firm or company, or sometimes even outside the company. I have already discussed case of a unit which diverted large funds to other line of activity, in Chapter on case studies - Case Study No.3. It may here be mentioned that diversion of funds to other activities or product line is not necessarily an undesirable activity, but a necessity for survival of a unit in this age of obsolescence. But what is necessary is proper planning of such diversification activity and to take one's banker into confidence. According to Donaldson (42) the financial executive's primary responsibility is to preserve the continuity of the flow of funds so that no essential decision of top management is frustrated for lack of corporate purchasing power.

(42) Gordon Donaldson
"Strategy for Financial Emergencies"
While taking interviews of entrepreneurs I asked successful entrepreneurs to state the reasons or factors that have contributed to their success. This was necessary, as in my opinion, to find out real causes of sickness, it is also essential to know the reasons or factors that have contributed to the success of a unit. Many successful entrepreneurs gave such factors, but some were unable to say anything. I have given on the next page various reasons given by different 30 entrepreneurs, for their success in the line. It may please be noted that in the frequency column I have given the number of times the same factor was stated by different entrepreneurs.
### TABLE - X-C

Factors contributing to success of a unit.

<table>
<thead>
<tr>
<th>Reasons or factors that have contributed to the success of a unit</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>1) Right choice of the product taking into consideration need of the community. Innovations/changes made from time to time in the product to suit changing market requirements.</td>
<td>1 1 1 1 1 1 1 1</td>
</tr>
<tr>
<td>2) Quality of products being maintained.</td>
<td>1 1 1 1 1</td>
</tr>
<tr>
<td>3) Proper Financial Management - good amount of retained earnings for strengthening capital base.</td>
<td>1 1 1 1 1 1 1</td>
</tr>
<tr>
<td>4) Favourable market conditions, and/ or marketing capabilities &amp; set-up.</td>
<td>1 1 1 1 1 1 1</td>
</tr>
<tr>
<td>5) Proper labour management /</td>
<td>1 1 1 1</td>
</tr>
<tr>
<td>6) Proper production planning.</td>
<td>1 1 1 = 3</td>
</tr>
<tr>
<td>7) Proper management of the unit and team-work.</td>
<td>1 1 1 1 1 1 = 6</td>
</tr>
</tbody>
</table>

- 269 -
TABLE X-C (contd..)

<table>
<thead>
<tr>
<th>Reasons or factors that have contributed to the success of a unit</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>8) Partners/directors with diverse experience, co-ordination amongst partners.</td>
<td>1 1 1 1 1 = 7</td>
</tr>
<tr>
<td>9) Sincere hard work.</td>
<td>1 1 = 2</td>
</tr>
<tr>
<td>10) Support from banks</td>
<td>1 1 = 2</td>
</tr>
<tr>
<td>11) Availability of technical expertise.</td>
<td>1 = 1</td>
</tr>
</tbody>
</table>
It will be observed from Table No. X-C that right choice of product, timely innovations in the product to suit market conditions, favourable market conditions and marketing capabilities and set-up appear to be the most dominant reasons contributing to the success of any industrial unit. Other important factors are maintenance of quality of products, diverse experience of partners, and proper management of the unit.

An analysis of causes of failure or sickness of industrial units has already indicated that marketing is the most crucial factor which makes a unit sick. Now in the above analysis of successful units, we have seen that favourable market conditions, proper selection of product etc. make a unit successful. But even in the area of marketing, the right choice of product taking into consideration needs of the market and innovations or changes in the product, is the most crucial factor behind success of any unit. But unfortunately while selecting a product line, importance is not given by entrepreneurs to market study and research. I am aware that for making such market analysis and research for the purpose of selection of proper product line, there is dearth of market information and unless this gap of market information is removed, units would continue to commit mistakes in selection of product line and would become sick in due course. I have already made a suggestion in Chapter No.VIII to develop such market information system, with the
help of computers. I think that development of such information system is an important solution to the problem of growing sickness. However, till such market information is available on a national basis, entrepreneurs themselves should try to make their own market study and then only select a proper product line.

I think that so far in India the problem of sickness has been approached primarily from a financial point of view. Banks, government agencies and the sick units themselves have almost invariably focussed their analysis and their actions on issues of financial management, capital restructuring, cash loss financing, bank credit facilities and working capital management. The Tiwari Committee has recommended that viability on a commercial basis should be the main criterion for undertaking rehabilitation of a sick industrial unit. In my opinion, (which is based on study of 66 small scale industrial units) commercial viability of any unit depends mainly on marketability of its products and its marketing capability. Unfortunately, perhaps the importance of marketing has so far not been recognised much by previous researchers and study groups/committees. I am aware that an industrial unit can become sick due to interplay of a number of causes and all such

causes affecting a unit should be considered in the package of rehabilitation for successful revival of the unit. If marketing base of a sick unit is weak and it cannot be strengthened by a package of rehabilitation assistance, attempt of banks/financial institutions to revive the unit would be futile. My study shows that 80 per cent of the units become sick due to marketing problem. Therefore while supporting sick industrial units banks should try to make proper appreciation of market demand. It should be noted that attempts to reconstruct or rejuvenate sick enterprises without adequate thinking about marketing problems are likely to see short term success at best or most likely will result in protracted recurrence of sickness till the unit ultimately collapses.