CHAPTER V

SICK UNITS IN INDUSTRIAL ESTATE - CASE STUDIES
The small scale sector is the second major contributor to the industrial economy of India. It accounts for 95 per cent of the country's factory ownership, contributes nearly 49 per cent (Rs. 41.620 crores) of the total industrial production and exports from this sector exceed Rs. 2,250 crores accounting for 26 per cent of total Indian exports at present. Besides, this sector provides employment to 75 lakhs and indirect employment to millions.

But everything is not smooth within the small scale sector. Industrial sickness in India is rampant and is growing at an alarming rate and unmanageable. It is continuously on the rise and there is no sign of an abatement. Bank funds blocked in financing ailing industrial units in the country rose from 3,000 crores by June 1984 to Rs. 4,200 crores by the end of January, 1986. There were 92,015 sick small industrial units in the country at the end of December 1984, involving bank credit to the extent of Rs. 879 crores as compound with 81,647 sick units involving bank finance of Rs. 788 crores in June 1984,¹ and as compound with 26,000 sick units in December 1981 involving bank finance of Rs. 359 crores. But the sky figure claimed by the Federation of Association of Small Industries is

¹. Annual Report, Reserve Bank of India, 1984-85.
as high as 5,00,000. Though the small is beautiful, it is not always profitable. The phenomenon of industrial sickness has not affected India alone rather it has become a global phenomenon. Oil price hike, energy crisis, industrial recession, inflation, unemployment and fast changing technology are the reasons for the sickness and closures of hundreds and thousands of small and medium industries in the world. Growing incidence of industrial sickness in India is associated with the rapid growth of industries during the first four Five Year Plans. The dimension of industrial sickness especially in the small scale sector became somewhat noticeable in the early 70's with the census of small scale units in the country and since then there has been increasing trend causing serious concern to the government, the Reserve Bank of India, the banks and financial institutions.

EFFECT ON SICKNESS:

Industrial sickness has grave socio-economic concerns. It leads to unemployment, loss of production, under utilisation of productive assets, blockage of the savings of the community. Thus, a vicious circles is

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built into the economy. Industrial sickness adversely affects the morals of the entrepreneurs, banks, financial institutions, general public and governmental authorities. Because of all these adverse effects of sickness, it is the interest of all parties i.e., government, banks, financial institutions and entrepreneurs that the magnitude of sickness should be minimised as quickly as possible. It has caused deep anxiety among the entire commercial banking system. Huge funds are blocked in the assets of the sick units, as a result the banks not only loose the interest on the loan on recurring basis, but also opportunity of relending and hence argumenting their revenue further. So banks, the citadel of commercial credit have now become intensive care wards for critically and terminally ill industries.3

**DEFINITION:**

From a common man's common sense point of view a sick unit is one which is not healthy. A healthy unit is a unit that assures a reasonable return on capital and reserves after providing for depreciation (and reasonable remuneration for the proprietors or working partners in

a partnership firm). Reasonable rate of return can be determined on the basis of existing market rate.

Commercially, a sick unit is one which does not fulfil minimum standard of productivity and profitability due to internal shortcomings while other units in the industry are flourishing.

The Development Commissioner, Small Scale Industries conducted the National Census of Small Scale Industries during the year 1973. For this purpose, a sick unit was defined as one in which capacity utilisation was 20 per cent or less. The definition was based on capacity utilisation.

Some of the definitions given from bankers' point of view are given below.

i) The State Bank of India in 1972 defined a sick unit as a unit which is chronically irregular and required a study to evolve a nursing programme and close follow up.

ii) The study team of State Bank of India defined a sick unit as "a unit while fails to generate internal surplus on a continuing basis and depends for its survival and frequent infusion of external funds".

iii) Reserve Bank of India defined a sick unit as 'a unit which is incurring cash losses'.

'A unit which does not perform its primary functions - production, sales, collection of debts and repayment on debts in the normal way for reasons beyond the control of the management' can also be called as a sick unit.

By analysing the above definitions for the purpose of this study a sick unit was taken as one in which capacity utilisation was 20 per cent or less.

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CAUSES OF SICKNESS:

The causes of sickness are classified under two broad categories by Nagaraj and Srinivasan. They are external causes and internal causes. The external causes are - a) Government policies, b) Sudden and wide fluctuations in the demand for the product, c) Shortages and irregularity in the availability of raw materials, d) Continuous rise in cost of production and distribution, e) Inability to execute the project according to schedule, and f) procedural delays resulting in long gestation period etc.

The internal causes have again been divided into four categories viz., a) Marketing, b) Production, c) Financing, and d) Organisation.

1. Marketing Problems: These problems comprise of
   i) Inadequate and improper assessment of demand.
   ii) Poor quality of the product and technical incompetence.
   iii) Irregular deliveries.
   iv) Poor marketing efforts.
   v) Obsolescence.
   vi) Recession.

2. **Production Problems include:**
   i) Machine breakdowns, poor maintenance, poor quality of machines.
   ii) Poor quality of raw materials.
   iii) Poor labour productivity.
   iv) Power shortages.
   v) Lack of production planning and control.
   vi) Delayed supplies from sub-contractors.
   vii) Poor industrial relations.

3. **Financial Problems:** These include -
   i) Absence of proper accounting system.
   ii) Deliberate diversion of funds.
   iii) Poor collections.
   iv) Unplanned payments to creditors.
   v) High inventories.
   vi) Poor working capital management.

4. **Organisational Problems:** These include -
   i) Lack of risk taking entrepreneurship.
   ii) Differences of opinion among partners/family disputes.
   iii) Delay in sanction of working capital limit by banks.
   iv) Strikes, lockouts, natural calamities.
   v) Change in Government policy.
   vi) Lack of co-ordination.
MEASURES TO ARREST SICKNESS:

It is quite often said prevention is better than cure. Therefore, wisdom lies in prevention of the industrial sickness. For this purpose, the developmental corporations like government departments, financial institutions, commercial banks, infrastructure corporations who provide land, water, power, sheds, Small Scale Industrial Development Corporations, District Industries Centres should take lead to nurse and rehabilitate sick units. Some measures are mentioned below to reduce industrial sickness.

1) The man behind the project plays a predominant role in the sickness of the enterprise. Particularly, in the case of 1st generation entrepreneur, the agencies to finance the enterprise have to select very carefully with a thorough screening mechanism.

2) The project appraisals are to be more realistic with the best standards of appraisals.

3) District Industries Centres consultancy agencies promoted by IDBI, SISI, should take the responsibility for the industrial sickness.

4) Wherever additional funds are proposed to be pumped into Small Scale sick units by the Corporation, the development agencies should conduct a thorough cost
management audits with the help of qualified cost accountant and then only release the funds.

5) Regular visits by the representatives of banks or financial institutions to units assisted by them with a view to ensuring their proper monitoring.

6) Timely assistance can be given by simplifying procedures and formalities to release funds.

7) Industrial Reconstruction Corporation of India (IRCI) was established in April 1977 as a specialized financial institution to provide financial assistance for the reconstruction and rehabilitation of sick industrial units. IRCI was jointly promoted by the IDBI, ICICI, IFCI, LIC, SBI and other nationalised banks.

There is no specific formula for the cure of a sick unit. Each case will have to be diagnosed and proper remedies found for it. Industrial revival has become a major aspect of industrial development strategy in India. But the concessions to sick units must be rationalised. Otherwise, these concessions may lure successful units also by branding as sick units merely to draw concessions. Many measures have been initiated by the government but the problems of sickness continues as ever. This warrants an indepth study of sickness so that the planners and policy makers can get to the crux of the problem. There is no
doubt that the problem of sickness especially in the small industry sector is attracting increased attention from economists, politicians and policy makers. It, however, needs to be seen when really we would be able to find a solution to it.

PROFILE OF SICK UNITS:

1. Welfit Enterprises:

Welfit Enterprises located in Rural Industrial Estate is a proprietary organisation manufacturing cycle spokes, nipples and washers since 1988. This is employing the services of only three unskilled labour locally available. They are appointed temporarily. This is not a labour oriented unit. It is selling 60 per cent of its products within the State and 40 per cent of products outside the State. The working capital is provided by the personal investment and the secured loans from commercial banks. During the three years it has taken loans of Rs. 82.26, 76.28, and 52.68 lakhs. This does not mean that the business is progressing. The rate of return is positive during 1988-89 and it has become negative in succeeding years.

Throughout the three years, it is having negative net current assets only. It is suffering from the problems -
non-availability of raw materials, non-availability of funds. These two problems are leading for the contraction in production. Any how they are following the measures like purchasing raw materials in advance and also taking loans from private individuals and institution to safeguard the position of working capital. They are planning to purchase a generator, increase the production capacity. But due to the lack of liberal financial sanctions from the funding institutions, this unit is moving towards gradual sickness.

By an observation of the transactions of economic performance of the unit the following details are identified from the Table 5.1.

The K/L, S/L ratio is gradually declining. The K/L ratio varied from Rs. 25, Rs. 273 to Rs. 15,812.33 S/L decreased from Rs. 1,60,286.67 to Rs. 1,37,556.67. But the capital productivity remained growing from 6.34 to 8.69. When compared, the net profit to sales varied 2.39 to 2.73. The current ratio did not reach the standard of 2:1 never since its inception. It is 0.61, 0.75 and 0.70 during the period under study. Similarly the quick ratio did not reach the standard of 1:1. It is 0.24, 0.23 and 0.32. This lack of reaching the standard ratio stands as the gospel of the sickness of the unit.
TABLE 5.1
DIFFERENT INDICATORS TO MEASURE THE ECONOMIC PERFORMANCE OF UNIT WELFIT ENTERPRISES

<table>
<thead>
<tr>
<th>Sl. No.</th>
<th>Indicators</th>
<th>1988-89</th>
<th>1989-90</th>
<th>1990-91</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Capital per Worker (K/L)</td>
<td>25,273.00</td>
<td>22,237.67</td>
<td>15,812.33</td>
</tr>
<tr>
<td>2</td>
<td>Labour Productivity (S/L)</td>
<td>1,60,286.67</td>
<td>1,57,586.67</td>
<td>1,37,556.67</td>
</tr>
<tr>
<td>3</td>
<td>Capital Productivity (S/K)</td>
<td>6.34</td>
<td>7.09</td>
<td>8.69</td>
</tr>
<tr>
<td>4</td>
<td>Output-Input Ratio (Sales-Purchases Ratio)</td>
<td>0.83</td>
<td>0.94</td>
<td>1.41</td>
</tr>
<tr>
<td>5</td>
<td>Gross Profit to Sales</td>
<td>15.01</td>
<td>15.00</td>
<td>15.00</td>
</tr>
<tr>
<td>6</td>
<td>Net Profit to Sales</td>
<td>2.39</td>
<td>(-)</td>
<td>0.40 (-)</td>
</tr>
<tr>
<td>7</td>
<td>Current Ratio</td>
<td>0.61</td>
<td>0.75</td>
<td>0.70</td>
</tr>
<tr>
<td>8</td>
<td>Quick Ratio</td>
<td>0.24</td>
<td>0.23</td>
<td>0.32</td>
</tr>
</tbody>
</table>

Source: Field Survey.

a. Standard Ratios: Current Ratio: 2 : 1 ; Quick Ratio: 1 : 1
b. Capital per Worker = \frac{\text{Capital}}{\text{Labour}}
c. Labour Productivity = \frac{\text{Sales}}{\text{Labour}}
d. Capital Productivity = \frac{\text{Sales}}{\text{Capital}}
e. Output, Input Ratio = \frac{\text{Sales}-\text{Purchases}}{\text{Sales}}
f. Gross Profit Ratio = \frac{\text{Sales} \times 100}{\text{Gross profit}}
g. Net Profit Ratio = \frac{\text{Sales} \times 100}{\text{Net Profit}}
The growth in the administrative costs, ups and downs in the market and lack of pre-investment planning are the three main and solid reasons for the sinking state of this unit with its apparent sickness since its inception.

2. Vijay Industries:

Vijay industries located in Chowlur village is outside Industrial Estate. This is producing tooth powder since 1985. They are employing the services of 12 local unskilled labourers on temporary basis since three years. They are using preceptate calcium carbonate as a main raw material. They are having a ribbon blender mixer as a main plant. They are selling their product within the State only. The sales value increased from ₹. 2,08,460 to ₹. 2,50,592.

They are getting the funds by secured loans from commercial bank. It is on an average about ₹. 3,90,000 per annum. This institution is having negative rate of return during 1989-90 and 1990-91. This institution is neither having the contraction in demand nor problems like raw material supply. They are having only labour problem and absence of market data. In order to cross over the problems they are planning to improve the production and diversifying the varieties of product and the modernisation of machinery.
## TABLE 5.2

DIFFERENT INDICATORS TO MEASURE THE ECONOMIC PERFORMANCE OF UNIT VIJAY INDUSTRIES

<table>
<thead>
<tr>
<th>Sl. No.</th>
<th>Indicators</th>
<th>1988-89 (Rs.)</th>
<th>1989-90 (Rs.)</th>
<th>1990-91 (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Capital per Worker (K/L)</td>
<td>3,092.25</td>
<td>2,467.08</td>
<td>1,614.25</td>
</tr>
<tr>
<td>2</td>
<td>Labour Productivity (S/L)</td>
<td>17,371.67</td>
<td>20,039.17</td>
<td>20,882.67</td>
</tr>
<tr>
<td>3</td>
<td>Capital Productivity (S/K)</td>
<td>5.62</td>
<td>8.12</td>
<td>12.94</td>
</tr>
<tr>
<td>4</td>
<td>Output-Input Ratio (Sales-Purchases+Dep Ratio)</td>
<td>1.28</td>
<td>1.37</td>
<td>1.23</td>
</tr>
<tr>
<td>5</td>
<td>Gross Profit to Sales</td>
<td>19.99</td>
<td>20.01</td>
<td>20.00</td>
</tr>
<tr>
<td>6</td>
<td>Net profit to sales ratio</td>
<td>1.49</td>
<td>(-) 0.62</td>
<td>(-) 1.69</td>
</tr>
<tr>
<td>7</td>
<td>Current Ratio</td>
<td>1.25</td>
<td>1.22</td>
<td>1.09</td>
</tr>
<tr>
<td>8</td>
<td>Quick Ratio</td>
<td>0.66</td>
<td>0.78</td>
<td>0.79</td>
</tr>
</tbody>
</table>

Source: Field Survey.

Standard Current Ratio: 2:1
Standard Quick Ratio: 1:1
From the Table 5.2, the following details of economic performance are identified; the K/L ratio is declining from Rs. 3,092.25 to Rs. 1,614.25 during the period under study. Whereas the S/L is increasing from Rs. 17,371.67 to Rs. 20,882.67. Similarly S/K is also increasing from 5.62 to 11.94. The gross profit to sales ratio is increasing from 19.99 to 20.00. But the net profit ratio is suffering from the negative result during 1989-90 and 1990-91. Both the current ratio and quick ratio have never reached the respective standard ratios of 2:1 and 1:1.

The above situation indicates that the net result is some degree of sickness with the unit. That is promoted by the reasons like other business activities of the entrepreneurs, acquisition of fixed assets, problems of labour, and also growth in the selling and administrative costs.

It is apparent that the sickness of Welfit, which is located inside Industrial Estate, is more high making it a misfit when compared with the Vijay Industries situated outside Industrial Estate.

CONCLUSIONS:

From these two case studies the following points are observed.
It will be seen that the causes for sickness in units, Vijay Industries and Welfit Enterprises are labour trouble, mismanagement, and market ups and downs. But a close look at the profiles shows that these are apparent causes which are seemingly responsible for the units to got red. There is something else to be blamed for.

Unit Welfit Enterprises, it will be noted, is not been having a smooth sail right from its inception. There are ups and downs in its career because it did not pass through the usual preinvestment planning process.

The problem of labour brought out by manager in unit Vijay Industries, is the apparent cause of sickness. The labour trouble in the surface and the failure of the entrepreneur to build reserves, instead of ploughing profits into acquiring fixed assets, preceded the event of rejection of products. Rejection of products can only be the actual cause for sickness in this unit.

The ups and downs in the fortunes of Welfit Enterprises, problems of labour and acquisition of fixed assets in Vijay Industries instead of building reserves, be called the originating factors on account of which the apparent factors came out and the units were led into sickness. That, however, is not the whole story any way. Once the units went into red there was a chance of their coming
out if had the banks extended credit in time. Bank accommodation would have acted as a saving factors but the bankers did not come to the rescue of the units. When the banks failed to come to their rescue the entrepreneurs adopted, what may be called the survival strategies, such as borrowing in open market, liquidation of assets, etc.

Whether or not entrepreneurs of the units under study will succeed in retrieving the units from red is yet to be seen. But, by now it is clear what the process of sickness would be like. Thus to trace this process, there is always an originating factor which is less apparent but works slowly to bring the apparent causes to surface. The saving factor could provide the needed cushioning to the unit but if this is not forthcoming the entrepreneur would try some survival strategies in desperation. This process of sickness is traced in Table 5.3 with reference to the units studied. It will be seen that the originating the apparent factors and the survival strategies vary across the units but the saving factor remains the same i.e., bank finance failing to turn up in time.

What brings into picture the originating and the apparent factors? And what makes the banker not to come in time to help the sick units? Why does the entrepreneur adopt the new survival strategies? The answers
to these questions lye in the environment in which the industrial units are operating.

**TABLE 5.3**

**PROCESS OF SICKNESS IN THE UNITS UNDER STUDY**

<table>
<thead>
<tr>
<th>Name of the Unit</th>
<th>Originating Factors</th>
<th>Apparent Factors</th>
<th>Saving Factors</th>
<th>Survival Strategies</th>
</tr>
</thead>
<tbody>
<tr>
<td>Vijay Industries</td>
<td>Market recession, Labour problem of Labour, Acquiring fixed assets.</td>
<td>Bank liquidation of assets, borrowing credit from friends and private institutions.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Welfit Enterprises</td>
<td>Ups and downs in fortunes, owing to lack of pre-investment planning.</td>
<td>Labour problem</td>
<td>Bank credit</td>
<td>Switch over to new products, modernisation of machinery.</td>
</tr>
</tbody>
</table>

It is well-known fact that the small industries hardly carry out pre-investment project planning and evaluation studies and assess the situation in input and product markets before going into business. There is a practice among the small industrialists whereby they go straight into action without completing the "preliminaries" which would give them a picture of the prospective returns, problems in procuring inputs and selling the finished product,
possibility of unsold inventory accumulation and so on. Welfit Enterprises is a typical case of such an unplanned enterprise which has been having its ups and downs right from its inception.

The sharp rise in the prices in the early 1980's and the consequent rise in labour and trade union militancy in the country had led to an unprecedented deterioration in industrial relations situation. The time-loss due to work stoppages reached the peak of 60 million mandays in 1964. This culture of work stoppages, which was by and large the monopoly of the large and medium scale industries till recently, appears to have now percolated to the small units too. Vijay Industries and Welfit Enterprises seem to have been influenced for the movements of labour militancy, in the neighbourhood.

The banker, against whom there is complaint of non-compliance at times of need, also works in an environment which has forced him to be cautious and reluctant. It will be noted that large amounts of bank credit advanced to industries have been locked up and by May 1985 the funds so locked up with large, medium and small scale industries:

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worked out to be ₹ 3,081 crores. In a situation of heavy locking up of funds in the sick units it is but natural for the bankers to be reluctant to provide further funds to the sick units. That is why bankers did not oblige when Vijay Industries and Welfit Enterprises approached for further credit.

Moreover, the survival strategies followed by the entrepreneurs hint at a new management culture that is emerging in the small industries sector. There are complaints that many of the small industry owners feign sickness in order to obtain Government assistance and institutional finance. This strategy of 'somehow' obtaining benefits from the state is said to become part of the industrial culture in India. A perusal of the profile of sick units gives some credence to this theory. It will be seen that the entrepreneur of Vijay Industries has different concerns which are doing well. This fact gives rise to the suspicion that he might be diverting finance to the new units thereby forcing sickness on this unit. Obviously, this is a gruse put by him to obtain institutional finance under the cover of sickness.

CONCLUSION:

Owing to the limitations of methodology the macro statistical studies can neither go deep into the
causes for industrial sickness nor capture the process of sickness. It was, therefore, felt that alternatively case study method may be followed to bring out the aspects of sickness which the statistical studies do not bring out.

The general elements of the process of sickness that emerge from the units under study are:

There are some originating factors which bring the apparent causes to surface. If bank finance comes in time the unit is saved. If not entrepreneur adopts some survival strategies which very often lead the unit further deep into sickness.

Lack of pre-investment planning, deteriorating industrial relations and perverse management culture that now pervade the small industry sector are the other reasons of sickness. An entrepreneur to succeed must be able to manage men, material and money. 'Men' includes not only the men employed in his industrial unit that is labour but also men concerned with the Government and funding agencies. Inability and inefficiency to deal with those three important factors associated with lack of motivation, diversified interest, result in under utilisation of capacity and dearth of working capital, cause sickness and failures in Small Scale Industry Sector.