

Dr MPS college of business studies

Subject : Business organization

Unit 2

Small Business Meaning

A business which functions on a small scale level involves less capital investment, less number of labour and fewer machines to operate is known as a small business.

Small scale Industries or small business are the type of industries that produces goods and services on a small scale. These industries play an important role in the economic development of a country. The owner invests once on machinery, industries, and plants, or take as lease or hire purchase. These industries do not invest more than one crore. Few examples of small-scale industries are paper, toothpick, pen, bakeries, candles, local chocolate, etc., industries and are mostly settled in an urban area as a separate unit.

Characteristics of Small Scale Industries

Ownership: They have a single owner. So it is also known as a sole proprietorship.

Management: All the management works are controlled by the owner.

Limited Reach: They have restricted area of operation. So they may be a local shop or an industry located in one area.

Labor Intensive: Their dependency on technology is very little because they are dependent on labours and manpower.

Flexibility: Because they are small, they are open and flexible to sudden changes, unlike large industries.

Resources: They utilize local and immediately available resources. They do better utilization of natural resources and limited wastage.

Categories of Small Business

On the basis of capital invested, small business units can be divided into the following categories:

(1) Small Scale Industry (Before 2006)

They invest in fixed assets of machinery and plant, which does not surpass than one crore. For export improvement and modernization, expenditure ceiling in machinery and plant is five crores.

(2) Ancillary Small Industrial Unit

This industry can hold the status of an ancillary small industry if it supplies a minimum 50 per cent of its product to another business, i.e. the parent unit.

They can produce machine parts, components, tools or standard products for the parent unit.

(3) Export Oriented Units

This industry can possess the status of an export-oriented unit if it exports exceeds 50 per cent of its manufactures.

It can opt for the compensations like export bonuses and other grants awarded by the government for exporting units.

(4) Small Scale Industries Owned by Women

An enterprise operated by women entrepreneurs in which they alone or combined share capital minimum of 51 per cent.

Such units can opt for the special grants from the government, with low-interest rates on loans, etc.

(5) Tiny Industrial Units

It is an Industrial or a company whose expenditure on machinery and plant does not exceed Rs. 25 lakhs.

(6) Small Scale Service and Business

It is a fixed asset investment on machinery and plant excluding land and building should not surplus Rs. 10 lakhs

(7) Micro Business Enterprises

It is a tiny and small business sector.

The investment in machinery and plant should not exceed Rs.1 lakh.

(8) Village Industries

The industries which are located in rural areas and manufacture any product performs any service with or without the utilization of power is called village industries.

They have fixed investments on capital as per head, workers, and artisan, which does not exceed Rs.50, 000.

(9) Cottage Industries

It is also known traditional or rural industries.

These industries are not covered by the capital investment criterion.

Cottage industries are characterized by the following features :

These are organized by a single, with private resources.
Use family labour and local talent.
Simple instruments are used.
Small capital investment is involved.
Simple products are made.
Indigenous technology is utilised.

Need for SMEs

- Steady and rapid growth of SMEs
- Develop new product and markets
- Produce quality goods
- Promote healthy development of human resources
- To develop SMEs on the successful track
- Provide credit support
- Marketing support

Role and importance of small scale industries in a developing economy:

1. **Employment generation:** Small scale industries are one of the best sources of employment generation in India. Employment is one of the most important factors that determines the growth of a nation. Therefore, development of small scale industries should be encouraged for the development of more employment opportunities in the nation.
2. **Less Capital Requirement:** Small scale industries are less capital intensive than the large scale industries. Capital is scarce in developing countries like India and therefore, small scale industries are most suitable for maintaining the balance.
3. **Use of resources and development of entrepreneurial skills:** Small scale industries allow for the development of entrepreneurial skills among the rural population which is not having the scope of large scale industries. These industries help in the appropriate use of the resources available in the rural areas, which leads to development of rural areas.
4. **Equal income distribution:** Small scale industries by generating employment opportunities create equal income opportunities for the youth of the underdeveloped areas. This leads to the growth of the nation in terms of employment, human development.
5. **Maintains regional balance:** It has been seen that large scale industries are mostly concentrated in the large cities or restricted to areas which leads to migration of people in search of employment to these cities. The result of such a migration is overcrowding of the city and damage to the environment. For sustaining a large population, more of natural resources need to be utilised.
6. **Short production time:** Small scale industries have a shorter production time than the large scale industries which results in flow of money in the economy.

7. Supporting the large scale industries: Small scale industries help in the growth of the large scale industries by producing ancillary products for the large industries or producing small components that will be useful for the assembling of final products by the large scale industries.

8. Improvement in Export: Small scale industries contribute to around 40% of the total exports done by India, which forms a significant part of the revenue earned from the exports. Small scale industries work towards increasing the forex reserves of the country that reduces the load on balance of payment of the country.

9. Reduce the dependence of agriculture: Most of the rural population will be dependent on agriculture and this creates a burden on the agricultural sector. Small scale industries by providing employment opportunities to the rural population provides more avenues for growth and also paves way for a more arranged distribution of occupation.

Problems faced by SMEs

1) Financial issues:

In the Indian economy, access to finance has always been an issue for smaller firms and businesses. This is a major hindrance for businesses as well as the SME sector. However, the most disturbing fact about it is that only 16% of SMEs get access to timely finance, resulting in small and medium firms being forced to rely on their own resources. It is not just small firms that face this problem, but larger firms do as well because even those bigger players face significant difficulties in accessing cheaper credit from formal banks.

2) Regulatory issues:

Several regulatory issues have been identified over time, including problems like tax compliance and changes to labor laws which have ended up costing the SME sector dearly. In an attempt to make this sector more competitive among others, certain labor reforms were attempted some years back. Still, they failed to make any dent in improving things for SMEs despite making them more competitive than larger firms. As a result, it has become very difficult for SMEs to comply with these regulations and register for tax compliance, which has resulted in many operating on low capital or even shutting shops.

3) Infrastructure:

In India, the infrastructure sector is extremely important because we are often referred to as the 'world's back-office' because so many works in this sector are carried out overseas. Applications such as eCommerce and BPO have created more jobs in low-wage countries like India.

4) Low productivity:

SMEs are not necessarily very productive, but they perform certain tasks that emit more value than they produce. Retailers sell consumer goods to end-users at relatively lower prices. In fact, SMEs may be very productive only when it comes to being cost-efficient and

are capable of creating high volume at very low costs. But given that their production is on a small scale with low margins, low productivity can put them at a disadvantage, especially when compared with larger firms.

5) Lack of innovation:

Indian SMEs are not very innovative, and the majority of the products that they produce are based on outdated technologies. There is a severe lack of entrepreneurs in this sector, which has prevented it from adopting new technologies and tools which have brought about significant changes in other sectors like eCommerce and call centers, etc. As a result, SMEs have had to struggle with outdated technology as well as low levels of productivity, especially when compared with larger firms.

6) Technical changes:

There has been no dearth of technical changes over time, and most industries have undergone some form of change in order to remain competitive. As a result, Indian SMEs have had to deal with some very important changes which have affected their growth potential. At first, there was a change in the ownership right of land, which has made the sector more prone to mismanagement and, with it, a fall in productivity.

7) Competition:

Due to various factors, such as the rise of eCommerce and the advent of globalization, bigger firms have forced SMEs out of their markets. However, this is not new because SMEs were facing competition from year one, but they could fight it off successfully compared to professional firms. In fact, SMEs continue to face competition in many areas, including agricultural machinery, garments, and tourism.

8) Skills:

When it comes to skills, Indian SMEs are far behind their counterparts in other countries because they depend heavily on the help of informal workers, who are not paid well and lack the technical skills which can help enhance productivity. As a result, smaller firms are forced to take up jobs that require low levels of skill and expertise, which further affects their growth prospects in the long term.

9) Lack of professionalism:

A majority of Indian SMEs lack professionalism despite being vital for larger industries' growth. As a result, they are highly prone to corruption and abuse of power, which has a huge impact on the productivity of their businesses.

10) Lack of standardized policies:

There are very few SME policies in India. As a result, there is no consistency when it comes to SME development as well as entrepreneurship promotion programs. However, positive progress has been made in Delhi over the years, but this needs to be done on a national

level so that Indian firms can become more competitive across the world for global companies and investors.

Public sector

Definition: The public sector of an economy is the sector that provides a range of governmental services, including infrastructure, public transportation, public education, health care, police and military services.

Importance of the Public Sector in the Economy

The public sector is important for the following reasons:

- It plays a key role in the economic development of a country
- It helps in providing essential services to the citizens
- It provides employment opportunities
- It helps in the development of infrastructure
- It encourages private investment
- It promotes exports

The public sector is the backbone of the Indian economy and it plays a pivotal role in its development.

Objectives of Indian Public Sector:

The objectives of the public sector in India can be divided into three categories:

Social Objectives: The public sector aims at providing basic goods and services to the citizens. It also provides employment opportunities and promotes economic development.

Economic Objectives: The public sector plays a key role in the development of infrastructure and encourages private investment.

Political Objectives: The public sector protects the interests of weaker sections of society and promotes exports.

Major Problems Faced by Indian Public Sector:

There are several problems faced by Indian public sector enterprises .they are

- **Managerial Problems:** The public sector is plagued by red-tapism, bureaucracy, and corruption. These problems have led to inefficiency and poor quality of products and services.
- **Financial Problems:** Public sector enterprises are often dependent on the government for their financial needs. This dependence has led to a lack of autonomy and accountability.
- **Operational Problems:** Public sector enterprises are often hampered by outdated technology and processes. This has led to low productivity and high costs.
- **Delay in completion**

- Faulty evaluation
- Labour problem
- Political interference
- Poor returns

The public sector in India has been facing several problems over the years. These problems have adversely affected its performance and efficiency.

Measures to be taken by the Public Sector to be Effective and Efficient are:

- There is a need for better planning and coordination between the various agencies of the government.
- The public sector needs to focus on its core competencies and outsource non-core activities.
- There is a need for more transparency and accountability in the functioning of the public sector.
- The public sector needs to adopt new technologies and processes to improve its efficiency.
- The public sector needs to be more customer-oriented in its approach.
- The public sector needs to reduce its dependence on the government for financial assistance.
- The public sector needs to focus on its strengths and improve upon its weaknesses.

Rationale

1. Need for a Planned Economy:

For speeding up the process of economic growth, there is need for economic planning through Five-Year Plans.

Through public sector enterprises, the Government can ensure planned development of the economy according to plan priorities – a task which cannot be expected to be performed by the private sector.

2. Building Industrial Infrastructure:

Industrial infrastructure is necessary for rapid industrialisation and economic growth of the nation. This infrastructure consists of very basic facilities like transport, communication, power, irrigation, electricity, oil and gas, construction of roads, bridges etc.

Projects of building infrastructure have a long gestation period with lesser return on investment and are not at all attractive to private sector businessmen. Hence the need for public sector to take up the task of building industrial infrastructure.

3. Basic and Heavy Industries:

Basic and heavy industries include – iron and steel, coal, power, cement, fertilizers, petroleum etc. These industries are necessary for industrial development. These require huge capital investment, which is beyond the capacity of private entrepreneurs.

4. Public Utilities:

Public utilities consisting of services like water supply, electricity, gas, public transportation etc. are necessary for people to lead a worth living life. The Government has to assume responsibility for providing such services to the public, at most reasonable prices, in the interest of public welfare.

5. Defence Production:

Defence production consisting of goods and services needed for the defence forces of the country cannot be left to the whims (i.e. desires) of the private sector. Hence, public sector is needed to take care of defence items production in the most responsible way in the interest of national defence.

6. Development of Backward Regions:

Private individuals are least willing to start industries in backward areas e.g. rural areas, hilly areas or otherwise neglected areas; because location of industries in such areas is not profitable at all, in initial stages. In view of the balanced regional development of the economy, Government itself starts setting up industries in such backward areas on its own initiative, cost and convenience.

7. Fuller Employment:

One of the biggest aims of public sector enterprises is to generate maximum employment opportunities in society, to help solve the serious and grave unemployment situation of the economy. Private enterprises also provide employment; but these do not emphasize on generating employment opportunities at the cost of their profit-earning techniques.

8. Surplus for Economic Growth:

The surplus generated by public enterprises is available to the Government for investment in programmes of economic growth. In fact, taxation alone cannot provide huge funds for developmental purposes.

9. Preventing Concentration of Economic Power:

Public sector enterprises keep a check on the monopolistic tendencies of the private sector; and prevent concentration of income and wealth in the hands of private individuals. In fact, good public enterprises are the biggest competitor for the private sector.

10. Socialistic Pattern of Society:

Under the Constitution of India, the Government is committed to achieving the goal of a socialistic pattern of society. For this objective, there is a need to assign a significant role to the public sector.

Forms of Public sector

1. Departmental Undertaking
2. Statutory Corporation
3. Government Company

1. Departmental Undertaking:

Departmental enterprises are established as departments of the ministry and are considered part or an extension of the ministry itself. They have not been constituted as autonomous or independent institutions and as such are not independent legal entities. These undertakings are under Central or State Government and the rules of Central/State Government are applicable. Eg. Railways

Features: The main characteristics of Departmental Undertaking are as follows-

- The funding of these undertakings comes directly from the government.
- They are subject to accounting and audit controls applicable to other govt. activities.
- The recruitment and conditions of employment are the same as any other employee directly under the government.
- It is subject to direct control of the concerned ministry.
- Accountability of such enterprise is to the concerned ministry.

Merits: Departmental undertakings have certain advantages which are as follows-

- These facilitate the Parliament to exercise effective control over its operations.
- These ensure a high degree of public accountability.
- The revenue earned is a source of income for the govt. as it goes directly to the treasury.
- National security is not at all at risk as it is under the direct control of the government.

Limitations: This form of organization has some drawbacks too, which are-

- It fails to provide flexibility.
- No scope for the employees and heads to take independent decisions.
- These enterprises fail to take advantage of business opportunities.
- There is red-tapism involved.
- It also suffers from a lot of political interference.

2. Statutory Corporation:

Statutory Corporations are public enterprises that are brought into existence by a Special Act of Parliament. The Act defines its powers and functions, rules and regulations governing its employees, and its relationship with government departments. It enjoys the legal identity of a corporate person and has the capacity of acting under its name.

Features: Statutory Corporations have certain distinct features, which are discussed below-

- These are set up under an Act of Parliament and are governed by the provisions of the Act.
- This type of organization is wholly owned by the state.
- These act as a corporate body and can sue or be sued, enter into a contract, and own property in its name.
- This type of organization is usually independently financed.
- These are not subject to the same accounting and audit controls applicable to other govt. departments.

Merits: This form of organization enjoys certain advantages in its working which are as follows-

- They enjoy independence in their functioning and a high degree of operational flexibility.
- Govt. interference in these types of organizations is less.
- They frame their policies and procedures within the powers assigned to them.
- It plays a vital role in economic development.

Limitations: This type of organization suffers from several limitations, which are as follows-

- All actions of a Statutory Corporation are subject to many rules and regulations.
- Government and Political interferences are always there in major decisions.
- corruptions exist.
- Any important decision or action is always delayed due to advisors appointed by the govt. in the corporation board.

3. Government Company:

A Government company is established under the Indian Companies Act and is registered and governed by the provisions of the Indian Companies Act. According to the Indian Companies Act 2013, any company in which not less than fifty-one percent of the paid-up share capital is held by the Central Government, or by any State Government or Government, or partly by the Central Government and partly by one or more State Governments, and includes a company which is a subsidiary company of such a Government company is called Government Company.

Features: Government Company has certain characteristics which makes them distinct from other forms of organizations. These are discussed as follows-

- It is an organization created by the Indian Companies Act 2013.
- It has a legal identity.
- The management of the company is regulated by the provisions of the Companies Act, like any other Public Limited Co.
- The employees of the organization are appointed according to their own rules and regulations.
- These companies are exempted from the accounting and audit rule procedures. An appointed auditor by the central or state govt. presents the Annual Report directly in the parliament or state legislature.

Merits: Government companies have certain advantages which are as follows-

- A separate Act in the parliament is not required to set up a Government Company.
- It has a separate legal entity, apart from the government.
- It enjoys autonomy in all management decisions.
- These companies provide goods and services at reasonable prices and curb unhealthy business practices.

Limitations: Despite the autonomy given to these companies, they have certain disadvantages-

- Since the Government is the only shareholder in some of the Companies, the provisions of the Companies Act are not of much relevance.

- As it is not answerable directly to the parliament, it evades constitutional responsibility which a company financed by the govt. should have.
- The management and administration of such companies rest in the hands of govt., so the main purpose of a Government company, registered like other companies is defeated.