



A Study on performance of Small and Medium sized Enterprise (SME's) in India and strategies for countering down performance Nationally/Globally

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ABSTRACT

Small and Medium sized Enterprise (SME) development is crucial for sustained and equitable development of the Indian economy. Evidence from more economically developed Asian nations demonstrates that SMEs have considerable potential for driving economic growth. With the advent of globalization, manufacturing SMEs across are facing increasing international competition and the need to improve quality and efficiency of output to match international standards to survive looks imminent. With globalization India has a serious threat of economy downturn which will be a shock for most SME's. Therefore this study to underlined the strategies for Indian SME s Countering repeated Global/Domestic Slow Down, The Study was carried out by means of Secondary Data and revealed that Indian economic intelligentsia have individually and collectively suggested ameliorative steps for saving the small and medium entrepreneurs. By planning to implement Cost optimization, Manpower Trimming, Avoidance Postponement of Expansion Plans and Additional Borrowings, Sourcing of Personal Investments, developing Customer Relationship, Optimization of Working Capital : Identification of Financially Strong Clients Factoring of Invoices Domestic L/C Discounting. The Indian companies would have to study the above mentioned solutions and seek extensive dialogue with their employees, customers, banks and share holders to implement each of the solutions from time to time in the near future.

Keywords: SME's, Entrepreneurs, Manpower Trimming, Customer Relationship, Personal investments, Effective Working capital, Clients Retention strategy

INTRODUCTION

Small and Medium sized Enterprise (SME) development is crucial for sustained and equitable development of the Indian economy. Evidence from more economically developed Asian nations demonstrates that SMEs have considerable potential for driving economic growth. Under the right conditions, entrepreneurs, regardless of background, can start and grow SMEs, generating profits and creating employment opportunities. SMEs drive industrial progress, improve an economy's ability to deal with shocks and are recognized as breeding grounds of innovation.

As elsewhere in Asia, SMEs make up the vast majority of businesses in India. Almost 40% of the nation's enterprises have between 10 and 100 employees, It is estimated that SMEs provide about two thirds of the country's employment.

With the advent of globalization, manufacturing SMEs across are facing increasing international competition and the need to improve quality and efficiency of output to match international standards to survive looks imminent. With globalization India has a serious threat of economy downturn which will be a shock for most SME's. The impact when it hits, almost paralysis the SME space.. The Indian business environment needs improved efficiency parameters built in and SMEs need nurturing to be able to compete with imports, globally unfavorable factors etc. Creating a level playing field to face the global economy downturn and encouraging SME development will not only enable Indian SMEs to compete successfully in their domestic market; it will also pave the way for their involvement in catering to the global market.

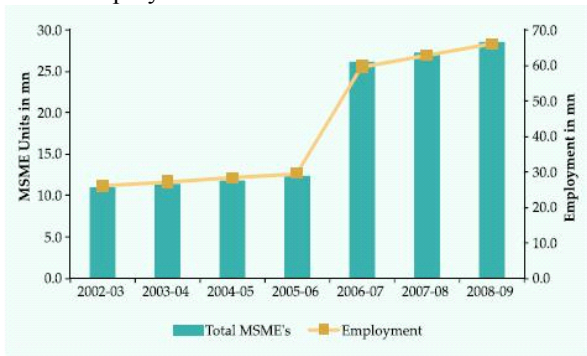
The Govt. of India has a stated commitment to private sector growth internally and globally . In this context it recognizes the added importance of SMEs for sustainable and equitable economic development. This report focuses on the growth and current status of Indian SMEs, and the main barriers they face for sustained development. It discusses a number of planned and implemented policies, and recommendations to encourage SME development when the global economy creates challenges as recession, economic slowdown and currency volatility.

THE ROLE OF SMEs In India

Micro, small and medium enterprises (MSMEs) play a crucial role in the development of emerging and developed economies. According to UNIDO, small and medium enterprises around the world are estimated to account for more than 90% of the total number of enterprises and 50-60% of total employment. In India, MSMEs contribute immensely to the economy in terms of output, exports and employment and thus have strategic significance. MSMEs account for nearly 45% of India's manufacturing output and more than 30% of total exports and provide employment to nearly 65.9 mn people, second to agriculture. With close to around 28.5 mn units in the sector, it is a driving force for long-term growth of the Indian economy.



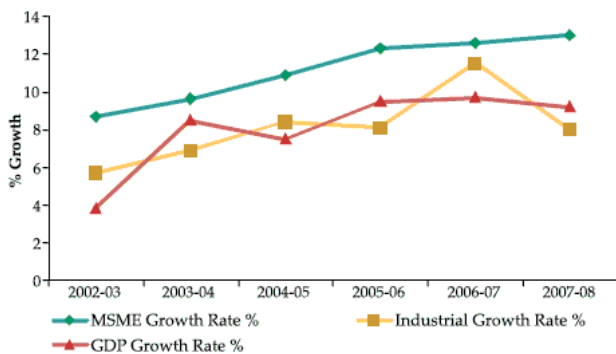
MSME employment and total number of MSME units



Source: Ministry of Micro, Small and Medium Enterprises, GoI
* Until 2005-06, data refers to the micro and small scale industry only. Data related to MSMEs was the industry and service sectors.

MSMEs performance

MSMEs outperformed IIP and GDP growth rates. The domestic MSME sector has grown at a much faster rate than industrial and GDP growth. In FY08, MSMEs total production at current prices (2001-02) was equivalent to about 16% of India's GDP (at current market prices). For 2007-08, MSMEs were projected to grow at 13% as compared to the industrial and GDP growth of 8% and 9.2% respectively. Over FY03-FY08, MSMEs recorded annual average growth of 11.2%, outperforming average industrial and GDP growth of 9% and 8% respectively. This is a clear indication of MSMEs' substantial contribution to the Indian economy through steady growth.



Source: Indiatat, D&B research

Total number and size of registered MSMEs (in thousands)

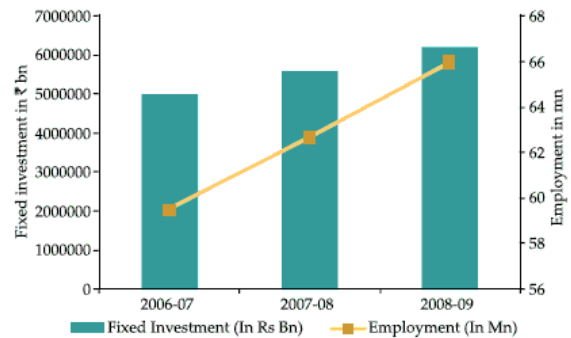
	Micro	Sm
Number of manufacturing enterprises	974.6	5
Number of service enterprises	501.1	1
Total	1,475.7	7

Source: Ministry of Micro, Small and Medium Enterprises, GoI

Total production of MSMEs for the year 2008-09 was ` 8,808 bn (at 2001-02 prices). During 2006-07 and 2008-09, the sector's total production grew at a CAGR of 11.4%. Fixed investment and employment in MSME on a growth trend MSMEs have experienced drastic improvement in productivity, which directly indicates the efforts in the sector to integrate the work force with technological enhancements to increase volumes. Production per employee in 2008-09 was at 0.13 mn, compared with 0.12 mn in 2006-07. Moreover, fixed investment grew more

than 11% y-o-y during FY08 and FY09. Employment on the other hand grew more than 5% y-o-y.

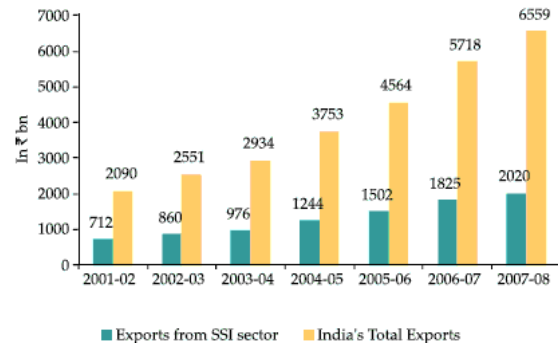
fixed investment and employment in MSMEs



Source: Ministry of Micro, Small and Medium Enterprises, GoI

SSI and India's total exports

MSME exports account for nearly one third of the country's total exports. MSME exports have managed to keep up with the growth rate of total exports of the country. The period of FY00-03 saw moderate growth in the economy, during which SSI exports grew in tandem with total exports at around 16% CAGR. Even during the boom phase (FY04-07), SSI exports kept pace with the CAGR of India's exports. However, during FY08, overall exports experienced much slower growth due to rupee appreciation, recording y-o-y growth of 15% in FY08, as against 25% in FY07. SSI exports also saw sluggish growth at 11% (versus 21% in FY07). Notably, since FY00, the share of SSI exports has been above 30% and stood at 31% during FY08.



Source: DGFT, MSME AR 09

A crucial industry segment as this needs measures to counter economic slowdown and look inwardly and outwardly to sustain and prosper.

PRESENT SCENARIO

The year 2011 has just ended but not the challenges which were faced by the industry in general and SMEs (Small & Medium Enterprises) in particular. The issues faced are largely due to the spiraling effect of global slow-down and a gloomy economic predication. The US and European economies are facing economic slow-down. The double dip recession kind of circumstance and falling Rupee has prompted a thought that exports from India will eventually be the casualty. Lot of policy implementing institutions in India have taken steps intended for course correction in the economy which includes higher interest rates, FII



investment revised rules and regulation which hinder the flow of inward investments and uncontrolled crude oil pricing which bears a detrimental effect for overall growth of the industry. These steps have inflicted heavy pressure on the performance of the Small and Medium Enterprises. Several organizations had to drastically alter their approach and literally hang in balance to avoid being badly hit by the situation. Nevertheless the businesses were able to survive only because they were ready to reinvent themselves. In this segment of the article we wish to dwell on the steps taken and how they have already impacted the enterprise.

Interest Rate

The year 2011 saw a soaring inflation of the Wholesale Price Index in India driven particularly by the spurt in demand of food items due to some contributory consumption factors. The Indian central bank that is the Reserve Bank of India came out with announcements to increase the Repo and Reverse Repo rates by several basis points within a gap of 2 quarters. This led to an immediate action of increasing the rate of interest by each and every individual Bank be it, nationalized or Private. Naturally, this enhanced rate of interest resulted in companies bearing the brunt of an increased, unplanned outflow resulting in a dent in the Balance sheet.

Delayed Receivables

SME's have been effected by late payments from Corporate (their biggest customers) as large companies are looking at the balancing act of payables ageing vis a vis increased rates from banks. This payment delay is due to the fact that most of them are short of confidence as they are inundated with information on global and domestic monetary crisis.

Consequence

Delayed payments and enhancement in sundry debtors for SME's have led to a difficult situation. The sourcing of raw materials has become difficult and companies face challenges in buying bulk raw material to enable improved costs. Inventory maintenance has faced severe imbalance due to improper off take of finished goods. The scenario ends in irregular salary payouts thereby creating non satisfied employees.

All the factors listed above has resulted in a financial disarray, causing enormous hardship particularly to the new SME entrants. Established Companies have also been straining every muscle to cross the budgeted top line and bottom line.

CUMULATIVE EFFECT

The Balance Sheets of many Organizations have turned negative which has caused a setback of their image with the shareholders. Many bankers are also reluctant to support such Companies and are not allowing excess borrowing or even the normal access to funds.

Retention of quality manpower, experienced technical personnel and old hands has been affected, thereby affecting the company culture and its working norms to do with qualitative parameters. This is in addition to 2010 not being an encouraging year and 2011 sustaining the slowdown with policy variations which has affected SME's operationally and commercially.

SOLUTIONS

Industry Concerns –SME Exchange-quite innovative and timely decision

1. The cost of raising capital for SMEs is quite high.

2. The current means of financing for SMEs are not adequate as they do not have easy access to funds from Angel Investors, VCs and PE players.

3. Most costs of compliance in raising capital under the existing guidelines are fixed. As a result, the costs become burdensome for smaller issues (SMEs).

4. The SMEs should be provided a framework that would enable them to raise capital quickly and at a low cost.

5. Owing to small size and less affordability, the eligibility conditions, listing requirements, corporate governance norms and disclosure standards may need to be suitably relaxed for SMEs.

In view of the aforesaid concerns raised by the market participants / industry representatives, there is a felt need for developing a dedicated stock exchange

for the SME sector so that SMEs can access capital markets easily, quickly and at lower costs. Such dedicated SME exchange is expected to provide better, focused and cost effective service to the SME sector. The need for having a separate exchange / platform for SMEs was also discussed during the 32nd Annual Conference of IOSCO held in April 2007 in Mumbai and it was felt that the same would be necessary for the focused development of the SME sector. Subsequent to the same, Today BSE(Bombay Stock Exchange) has made the initiative to start an exclusive SME exchange which will start functioning from April 2012. In addition to the above the following points should be kept in mind.

Amazingly, at this juncture, Indian economic intelligentsia have individually and collectively suggested ameliorative steps for saving the small and medium entrepreneurs. Most of these action plans are easy to implement, even while they will stall the cancer of downturn from impacting the industry as a whole. Some of these steps are enumerated below

- Cost Optimization :

This step is possible if the business is streamlined to snip off unproductive areas. Also, Most important thing that to be considered by SMEs are, the cost of borrowing, inventory management, effective working capital management and optimum manpower utilization & fast payment receipt by announcing certain incentives also to the buyer.. it would be important to have a sharp focus only on yielding revenue streams. In fact, this strategy is immediately applicable for the entire industry.

- Manpower Trimming :

Every Organization has excess flab to suit to the whims of some of the technical employees. If, manpower is wasted, or redundant, it would be wise to jettison it in Toto. The resultant reduction in cost would most definitely enhance profitability. SMEs should certainly consider in today's environment rather than future focus in employee



retention strategy, since running the company itself to today's situation becomes extremely difficult. The root to this is non implementation of tried and tested HR policies and measures. Entrepreneurs end up making emotional decisions which directly affects the enterprise in total. In other words, certain firm decision to be taken and should implement the same more vigorously to ensure the cost minimization.

- Avoidance of Additional Borrowings :

It would be necessary to exercise fiscal prudence and not involve in elitist expansion plans keeping long term goals in mind. In other words, the Companies need to become circumspect and indulge only in immediate unavoidable expenses. Implementation of processes to deal with this shall have long term gains. In other words, avoid paying excess interest for the operation, since the SMEs are already in margin pressure and adding up more interest will certainly dent the books of the company, which may become detrimental for the company in the long run, since the ratios of the project may become unviable for the banking institution to fund any expansion activity.

- Sourcing of Personal Investments :

The need of the hour is to cut high cost and medium cost debt on capital. A sure shot way of raising capital is through known sources and family. This shall enable a company to go improve their bottom line with current businesses. Lot of entrepreneurs when they are in crisis, they tend to borrow more money at relatively high cost for running the day to day operation and they always forget the fact that, adding more business partners and removing personal investment and transfer the same to the organization will definitely yield much better result in terms of operational viability. They should consider bringing in more money either by third party equity dilution or their own personal investment in to the business for safeguarding the business, as once the business gets stabilized, they can always draw more money from their and attain more wealth.

- Postponement of Expansion Plans :

As emphasized in point number 3, entrepreneurs have a tendency to gloat on past successes and end up making mistakes in a bad economy. This calls for seasoned set of advisors who can put the brakes on uncalled expansion. This is very important, as expansion is possible only after stabilizing the available business opportunities. Risky expansion could lead to disastrous consequences. In short span the cost of hiring the external consultants to analyze the operation may be a painful one. But if you neglect the same and start doing on your own method, it may lead to serious consequences and thereby make you to be in doldrums.

Global expansions are certainly not recommended at times of challenge. The large Capital Expenditure which involves maintenance of interest also would pose severe challenges to the very survival of the enterprise. Most of the global expansion planned, take place with old data and market available reports. Clear research and requirement parameters take a back seat. In most cases this has led to the parent entity also losing their visibility in the domestic market and end up squeezed for operational capital.

- Developing Customer Relationship : In order to expand order books, regular interaction with Star Customers is necessary. Optimization measures from the SME's side helps them cut costs on manufacturing thereby resulting in a more competitive pricing to sustain the existing customer. Also, prioritize the customer on their need and their payment capacity to us, so that, our working capital will not be blocked due to delay in payment.
- Optimization of Working Capital : A sense of tight rope walking must be practiced by the owners of the companies whenever working capital is being discussed. Clean management of working capital is possible only through scientific analysis of working capital and infusing just in time philosophy in their ranks and file. Preferably, the SMEs should work on the slot of innovative method of maintaining the working capital without disturbing the existing chain. Because, disturbance to the existing chain may become disasters in running the company.
- Identification of Financially Strong Clients : A conscious effort to define the pool of Elite customers who are available in the market would be required to strengthen profitability. Each Company must identify and develop their business with select set of clients who are good pay masters. Agreements may be signed to extend special facilities under attractive terms to enable them take quick decisions for a tie up with the Company.
- Factoring of Invoices :

This particular arrangement is not very much understood by the SME industry in India. It is possible to factor the invoices raised by a Company with its customer by entering into an repatriate arrangement with a discounting Organization. A tripartite agreement could be signed between the Company, the customer and the discounting Organization for factoring of invoices. Such an arrangement will ensure early receipt of the 90% payment for the Company which is being factored. This will ease the pressure for the organization as the effective management of working capital will make the company to run in much better environment. The discounting Organization will receive the payment from the customer at a later date in accordance to the agreement executed. Some among the institutions to be named are IFCI Factors Pvt Ltd, Can bank factors ltd etc



- Domestic L/C Discounting :

It is possible to extend this arrangement with the Bank of the Enterprise dealing with the Bank of the customer. Needless to say, this step is also not being widely used by the Small and Medium Enterprise. There is a need to sensitize the Enterprises to use Domestic L/C for reducing the impact of the fiscal pressure. SMEs should always try to get the facility with their own bank by way of paying some margin and keep the facility open for any future purchases and payments. SMEs can also recommend to their buyers to make the payment in LC, which in turn can be discounted with their own bank and avail the same for their business activity.

CONCLUSION

In 2012, the scenario in India for the Small and Medium Enterprise is one of promise. At the same time, it is also posing a plethora of challenges. To overcome this set of challenges and benefit from the immense opportunities, the Indian companies would have to study the above mentioned solutions and seek extensive dialogue with their employees, customers, banks and share holders to implement each of the solutions from time to time in the near future.

Corporate advisors and Mentors, need to be approached for counseling and hand holding to enable the entire SME sector to cross a large but not insurmountable hurdle. In any case, some of the Small and Medium enterprises from Retail, Pharmaceutical and Healthcare are slated to do well in 2012 which would be a repeat of their performance in the year 2011.

Government of India has also come out with a slew of measures and several plans to extricate the SME enterprises by cajoling the Banks to support the promoters in this hour of crisis. The effort to build the Brand SME India is commendable. One such praiseworthy move is the proposed launch of the much awaited SME Exchange from April 2012 (details has been provided in the initial column). This step will not only enhance confidence of investors and banks but will also allow equity from public to flow in to the companies. The 50 odd companies who are eventually listed will most certainly benefit but the others who are in the queue to get listed on the SME Exchange also stand to gain in a big way. The expected support from other institutions like MSME, NABARD and other institutions will certainly work on the welfare of the sector with the support from Government of India.

The future looks bright and will allow the evolution of companies to move quickly

to implement the steps described. It would be pertinent to recount that the rule of Corporate Evolution states that "The Fast" will stay and prosper, "The Slow" will be deprived and eventually perish. Therefore the pride of Indian SME story can be extended only if they are fast in implementing most of the action points explained in this article. Inexorable delay would lead to serious deprivation and slow death of the enterprise.

The situation would be retrieved by allowing the SME players to continue to make their yeoman contribution to the Indian Economy. The year of 2012 is without doubt, a year of challenges for the Indian SME champions but yet it is also one which will bring immense Business opportunities. That is exactly what many of the Captains of the Indian Industry believe. This Strong belief will lead eventually to irreversible success.

Limitations and Scope for future research:

As this study is based on Secondary data taken from the year 2000 onwards and studied only with India, there is a scope for future research by taking the data's universally so that the performance and positioning of SMS's all over the world can be discussed.

REFERENCE(Reference has been taken for only data in Image format and hence page numbers are not mentioned)

MSME employment and total number of MSME units

1. Source: Ministry of Micro, Small and Medium Enterprise, Government of India.

(Until 2005-06, data refers to the micro and small scale industry only. Data related to MSMEs was collected/compiled starting 2006-07 and hence includes both the industry and service sectors.)

Total number and size of registered MSMEs (in thousands)

2. Source: Ministry of Micro, Small and Medium Enterprise, Government of India.

MSMEs performance

3. Source: India stat, D&B research

Increase in estimated fixed investment and employment in MSMEs

4. Source: Ministry of Micro, Small and Medium Enterprises, Government of India

SSI and India's total exports

5. Source: DGFT, MSME AR 09