Write a brief note on Small Scale Industry

In most of the developing countries like India, Small Scale Industries (SSI) constitute an important and crucial segment of the industrial sector. They play an important role in employment creation, resource utilisation and income generation and helping to promote changes in a gradual and phased manner. They have been given an important place in the framework of Indian planning since beginning both for economic and ideological reasons. The reasons are obvious.

The scarcity of capital in India severely limits the number of non-farm jobs that can be created because investment costs per job are high in large and medium industries. An effective development policy has to attempt to increase the use of labour, relative to capital to the extent that it is economically efficient.

Small scale enterprises are generally more labour intensive than larger organisations. As a matter of fact, small scale sector has now emerged as a dynamic and vibrant sector for the Indian economy in recent years. It has attracted so much attention not only from industrial planners and economists but also from sociologists, administrators and politicians.

Definition of Small Scale Industry:

Defining small-scale industry is a difficult task because the definition of small-scale industry varies from country to country and from one time to the another in the same country depending upon the pattern and stage of development, government policy and administrative set up of the particular country.

Every country has set its own parameters in defining small-scale sector. Generally, small-scale sector is defined in terms of investment ceilings on the original value of the installed plant and machinery. But in the earlier times the definition was based on employment. In the Indian context, the parameter are as follows,

The Fiscal Commission, Government of India, New Delhi, 1950, for the first time defined a small-scale industry as, one which is operated mainly with hired labour usually 10 to 50 hands.

Fixed capital investment in a unit has also been adopted as the other criteria to make a distinction between small-scale and large-scale industries. This limit is being continuously raised up wards by government.

The Small Scale Industries Board in 1955 defined, "Small-scale industry as a unit employing less than 50 employees if using power and less than 100 employees if not using power and with a capital asset not exceeding Rs. 5 lakhs".

'The initial capital investment of Rs. 5 lakhs has been changed to Rs. 10 lakhs for sma industries and Rs. 15 lakhs for ancillaries in 1975. Again this fixed capital investment limit was raised to Rs. 15 lakhs for small units and Rs. 20 lakhs for ancillary units in 1980. The Government of India in 1985, has further increased the investment limit to Rs. 35 lakhs for small-scale units and 45 lakhs for ancillary units.

Again the new Industrial Policy in 1991, raised the investment ceilings in plant an machinery to Rs. 60 lakhs for small-scale units and Rs. 75 lakhs for ancillary units.

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THE NEXT GENERATION OF REFORMS

The following are ten recommended areas of special focus in the second generation of economic reforms:

1. Political Reforms for Good Governance;
2. Re-engineering the Role of the government;
3. Administrative and Legal Reforms;
4. Strategic Management of the Economy with a focus on knowledge-based HRD Activities;
5. Fiscal Prudence;
6. Agricultural Sector Reforms;
7. Industrial Restructuring;
8. Labor Sector Reforms;
9. Foreign Trade and Outward Investment Policies;
10. Financial Sector Reforms.

Political Reforms for Good Governance

Political reforms are urgently required in concert with economic reforms.[40] Both are essential to ensure good governance. A paradigm shift is required in the prevailing system of governance. Serving the people and putting their interests above the interests of the ruling elite must be the prime motivating force driving the reformed system of governance. Good governance can be ensured through the provision of an adequate quantity of public services and by improving their quality. Indian politicians need to become fully aware of the costs and benefits of economic reforms. Ruling politicians with limited terms in office are often guided by narrow and short-term motivations while formulating policies in the national interest. The Indian public at large also needs to be thoroughly educated on the inevitable need to bear short-term pain in order to reap the somewhat uncertain longer-term gains from economic reforms.

Economic reforms in the future must be more people-centered. They must be given a human face so as to continuously enhance the social empowerments of the poorer and most vulnerable sections of the society. They must be gender-sensitive to improve the status of women and girls. The burden of adjustment to structural reforms must be more heavily borne by the richer sections of the society. Appropriate electoral reforms, including state

[40] For a discussion of the required political reforms in India, see Subhash C. Kashyap, *Political Reforms for Good Governance: A Policy Brief* (New Delhi: Shipra Publications, 2003).

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funding of elections, will help to reduce the lobbying power of the entrenched vested interests.

Re-Engineering the Role of the Government

Reforms must be aimed at 'right-sizing' (often involving downsizing) the government. Governments must specialize in performing roles that they can perform better than free-market private enterprise. The government must expand its role in areas such as the provision of public goods, especially primary health, primary education and the creation of social infrastructures. The role of the Planning Commission must be changed to that of a strategic think tank. The mindset of the politicians and the administrators needs to be changed to accept the re-engineered role of government in the context of market-oriented economic reforms. The intensification of economic reforms at the state level needs to be given a higher priority in the future since most social services and infrastructural activities are primarily the responsibility of the state governments.

Administrative and Legal Reforms

No matter how good the design and intent of economic reforms, their success ultimately depends on efficient and speedy implementation through sensitive and responsive administrative and legal systems. Transparency and accountability must be guiding principles for the formulation and implementation of policies and procedures. Improved administrative systems should be devised to ensure that merit subsidies directly benefit the targeted (generally the underprivileged) sections of society. Legal support services should be made available with more public funding and must be strengthened to provide justice to genuinely aggrieved sections of society more quickly and affordably.[41] Second-generation economic reforms also must focus on changing the mindset of administrators (especially at the grass-roots level) and of the judiciary (especially at the lower level) to support administrative and legal reforms that synergize with economic reforms for maximizing social welfare.

Strategic Management of the Economy

Macroeconomic management must be dovetailed with a well-formulated strategic national vision for the economy for the year 2020 (and beyond). Clarity, transparency and accountability (through identifiable responsibility centers) with properly designed incentive (and disincentive) systems should be the guiding principles governing strategic management of the economy. An

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[41] See Subhash C Kashyap (ed.), *The Citizen and Judicial Reforms under Indian Polity* (New Delhi : Universal Law Publishing Company, 2002).

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appropriate code of conduct should be evolved and observed by economic actors under a new managerial system of governance. The strategic management of the Indian economy in the twenty-first century must focus on human resource development to promote knowledge-based and skill-intensive economic activities in line with India's dynamic competitive advantage.

Fiscal Prudence

The fiscal deficit (especially the revenue deficit) needs to be quickly reduced. India must sincerely implement the Fiscal Responsibility and Budget Management Act . Simultaneous action is required at both central and state levels to raise the tax-to-GDP ratio by expanding the tax base (for example, by taxing services and rich agriculturists) and improving tax administration (for example, through computerization). The revenue deficit must be brought to zero within five years.

Agricultural Sector Reforms

While some agricultural reforms have already been carried out, these are highly inadequate. Primacy must be given to the agriculture sector in all future reforms since many more jobs can be created in the agricultural sector, broadly defined, including activities related to rural industrialization and overall rural development. Both on-farm and off-farm employment potential must be fully exploited. This will raise incomes of farmers and rural labor on a sustainable basis and provide a much-needed boost to demand for industrial products and services, thus spurring all-around economic growth.

There is an urgent need to raise public investment in agriculture substantially. Areas needing investment include: irrigation; watershed development; rural infrastructure; drinking water; housing and sanitation. This will help raise the productivity of Indian agriculture to international levels and help in promoting rural (and interlinked urban) prosperity in India.

Second-generation reforms must reduce the perennial anti-agricultural bias by permitting free® exports of all primary products. This will provide a major boost to India's exports consistent with the rules set by the World Trade Organization. Simultaneously, India must improve its marketing infrastructure. Agricultural reform will unleash high growth rates in agriculture, on which nearly sixty percent of India's population is still dependent for employment. Agricultural prosperity will help to markedly reduce endemic rural poverty.

Industrial Restructuring

Industrial reforms must be geared to explicitly improve the productivity and international competitiveness of Indian industry by focusing on niche products and niche markets. Economic policy in this respect must facilitate

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mergers and acquisitions and the winding up of terminally ill enterprises in both the public and private sectors by restructuring bankruptcy laws. Massive restructuring is required of Public Sector Units. Most non-performing public sector units should be quickly sold through a privatization process that also safeguards the interests of workers through fair compensation for loss of jobs. Public sector enterprises should be governed by a commercial culture in which government holdings are no more than 26 percent of equity and are retained only to preserve strategic control. It is of the utmost importance that micro-level reforms must supplement macro-level reforms in the future to achieve synergy. The private sector in India needs to become more international in its outlook to become more competitive and to increase its overseas presence through outward FDI.

Labor Reforms

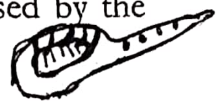
A properly formulated labor policy must form the core of second-generation reforms. This will require viable alternative social safety nets and effective retraining and re-employment opportunities. Once satisfactory safety nets are in place, more intensive competition should be injected into the labor market by allowing 'hire and fire' policies unambiguously linked to the productivity and profitability of micro-enterprises. The government should start by exempting units in the newly created Special Economic Zones from the rigors of labor laws. These measures would be of great help in redressing inefficiency of workers in public enterprises and public services (such as health care in rural areas).

Foreign Trade and Outward Investment Policies

No economic reforms can succeed in India without ensuring adequate growth of exports of goods and services to ensure longer-term viability of its balance of payments. While anti-dumping measures need to be strengthened to protect Indian industry from unfair import competition, the longer-term reforms must continue to lower import duties to levels comparable to those in leading Southeast Asian countries. Simultaneously, measures should be taken by the government to replace quantitative restrictions (wherever they still remain in place) through appropriately determined tariffs.

The second generation of economic reforms must facilitate the growth of India's own Multi-National Corporations (MNCs). The government must further liberalize outward foreign investment to allow potentially competitive Indian MNCs to establish production bases abroad and trade internationally.

Finally, industry and government must make cooperative efforts to prepare Indian industry to meet the new and ever-emerging challenges posed by the



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status.

Reforms and FDI flows

24 [With a progressively liberalized FDI policy regime since 1991 and a large and growing domestic market, among other advantages, the investment climate has steadily improved; it was only behind China and the US in 2005 and has stayed within the top three ranks since then. FDI inflows received by India have shown a marked increase since the 1991 liberalization, especially since 2001 as the Indian economy has picked up growth momentum. The big turnaround came in 2006 when the magnitude of FDI nearly tripled from $7.6 billion in 2005 to $20 billion. The inflows peaked at $40 billion in 2008 before declining to $35 billion in 2009 under the shadow of the global financial crisis.

The magnitude of FDI inflows received by India would appear small, especially if compared with inflows received by other countries in the region, such as China (around US$ 100 billion in recent years). However, the difference in the FDI to gross domestic product (GDP) ratio narrows if underestimation of FDI in India due to measurement problems and overestimation of FDI in China due to round tripping of Chinese capital are taken into account. The latter covers domestic Chinese investment registering as FDI through Hong

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Kong, Macau, or other countries to take advantage of a more favourable tax treatment of foreign investors. An analysis of the role of liberalization in explaining the rising FDI inflows suggests that only a part of the increase in FDI inflows in the 1990s could be attributed to liberalization, as the sharp expansion in the global scale of FDI flows also played a role. Further analysis suggests that liberalization of the FDI policy may be necessary but not sufficient for expanding FDI inflows. The overall macroeconomic performance continues to exercise a major influence onthe magnitude of FDI inflows by acting as a signaling device for foreign investors about the growth prospects of the potential host economy. Hence, paying attention to macroeconomic performance indicators, such as growth rates of industry through public investments in socio-economic infrastructure and other supportive policies, and creating a stable and enabling environment would crowd in FDI inflows. There has also been a discussion on the quality of FDI inflows in the post-reforms period. A substantial proportion of FDI in the post-reforms period has gone to services, infrastructure, and relatively low-technology intensive consumer-goods manufacturing industries largely oriented to India's domestic market and very little to export-oriented production. As much as 40 % of FDI in the late 1990s in India also took the route of acquisitions rather than green field ventures. In China, in contrast, FDI is concentrated in export-oriented and high-technology manufacturing industry and has come largely in the form of green field ventures.

Another important trend is India's emergence as a significant source of FDI flows. Although Indian companies have been investing abroad since the early1970s, the magnitude of investments was quite small until the mid-1990s. However, the magnitude as well as the number of outward investments started increasing since 2000 to around $1.5 billion per annum jumping to nearly $5 billion in 2005–6 and then to $14 billion in 2006–7. In 2007–8 the value increased to $19billion, before moderating slightly to $16 billion in the following year in the wake of the global financial crisis. In particular, involvement of Indian companies in large cross-border acquisitions, for example, Tata Steel-Corus, Hindalco-Novelis, and Tata Motors-Jaguar/Land Rover, among others, have helped in focusing attention on their emergence on the global scene. The recent spurt in the outward FDI activity of Indian enterprises reflects the change in motivation from purely market-seeking to also seeking strategic assets such as global brand names and marketing networks, proprietary technology, and other resources to jump-start their internationalization. Their ability to acquire much larger enterprises in the developed world despite their origins in a low-income country reflects their new found confidence in managing the acquired entities successfully. It has been argued that the source of their ownership or competitive advantage which enables such acquisitions lies in their accumulation of skills for managing large multi-location operations across diverse cultures in India and in their ability to deliver value for money.

Impact of FDI and the Role of Government Policies

Although the importance of FDI as a source of capital and output generation increased in the 1990s, its impact on domestic investment and growth is mixed as some FDI inflows possibly crowd in domestic investments while some others crowd it out. One way to maximize the contribution of FDI to host development is to improve the chances of FDI crowding in domestic investments and minimizing the possibilities of it crowding out

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domestic investments. In this context. **the experiences of Southeast Asian countries such as Malaysia, Korea, China, and Thailand in channeling FDI into export-oriented manufacturing through selective policies and export performance requirements imposed at the time of entry deserve careful consideration. Export-oriented FDI minimizes the possibilities of crowding out of domestic investment and generates favourable spillovers for domestic investment by creating demand for intermediate goods.** India's experience with respect to fostering export-oriented industrialization with the help of FDI has also been much poorer than that of East Asian economies. However, recent analysis suggests that MNEs are beginning to take a serious look at India's potential as a base for export-oriented manufacture.

Another policy that can help in maximizing the contribution of FDI inflows is to push them to newer areas where local capabilities do not exist as that minimizes the chances of conflict with domestic investment, as was done by Malaysia through pioneer industry programmes. **India is also attracting increasing attention from MNEs as a base for their knowledge-based activities, such as software development and global R&D activity.** Studies suggest that India's success owes largely to the cumulative investments made by the government over the past five decades in building what is now termed as national innovation systems, including higher education and centres of excellence, among other initiatives. Finally, in light of all this, it is clear that it is of critical importance for host governments to preserve policy flexibility to pursue selective policy or impose performance requirements on FDI, if necessary. Some of the performance requirements have already been outlawed by the World Trade Organization's (WTO) Trade Related Investment Measures (TRIMs) Agreement. Attempts have been made by developed countries to expand the scope of international trade rules beyond what is covered under TRIMs and the General Agreement on Trade in Services (GATS) and further limit the policy flexibility available to developing countries by creating a WTO multilateral framework on investment.

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