



FINANCIAL MANAGEMENT PRACTICES AND CHALLENGES IN SMALL SCALE INDUSTRIES

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Abstract

Small Scale Industries (SSIs) play a crucial role in the economic development of developing and emerging economies by generating employment, promoting balanced regional growth, and encouraging entrepreneurship. Effective financial management is vital for the survival, sustainability, and growth of these enterprises. However, SSIs often face numerous financial challenges such as inadequate capital, limited access to institutional credit, poor cash flow management, and lack of financial planning expertise. The financial management function is not a standardized operation. The functions vary from firm to firm depending upon the size of the company, nature of industry and tradition. Countries over the globe don't utilize a similar definition for grouping their Small and Medium Enterprise (SME) area nor completes an all-inclusive definition give off an impression of being vital. In India, the area has been by and large alluded to as the Micro, Small and Medium Enterprises. It also highlights the common financial problems faced by SSIs and suggests measures to strengthen financial efficiency and long-term viability. The study concludes that sound financial management practices significantly enhance profitability, stability, and competitiveness of small scale industries.

Keywords: *Small Scale Industries, Financial Management, Financial Problems, Practices, Cash flow.*

Introduction

In several countries, small-scale industries (SSIs) are the foundation of industrial development. They are currently widely categorized under the Micro, Small, and Medium Enterprises (MSMEs) sector in India. These businesses have a major impact on exports, GDP, and job creation. Many small-scale businesses struggle because of inadequate financial management systems, notwithstanding their significance. The planning, organizing, directing, and controlling of financial operations, including the acquisition and use of cash, is referred to as financial management. Effective financial management guarantees the best possible use of scarce resources, preserves liquidity, and boosts profitability for small-scale businesses.

Any purposeful organization's activities are significantly impacted by finance. The effective use of resources is the result of careful planning and management of company finances. Financial choices also affect the profitability or profits stream's size and fluctuation. Decisions in financial policy, including risk and profitability, impact the firm's worth. By providing the most amazing long-term incentive to the firm's protections, financial management's task is to achieve a balance between risk and production. As a result, financial management is crucial to the success and survival of commercial endeavors. The objectives of budgetary management are to increase the wealth, prosperity, and advantages of investors. In order to do this, the management must exercise caution while making decisions on finance, profit, and speculation. The fundamental managerial task that provides strategies for addressing deficiencies in various areas is financing. Therefore, financing is a crucial component of managerial duties and obligations that impact the operation of a firm. Additionally, the financial management would simply generate the funds required to buy the plant, equipment, and inventory, while the engineering and production team would identify the assets required to meet these demands. It is no longer common to operate in this manner. These days, financial managers are directly in charge of the control process, and

decisions are made in a much more coordinated manner. Therefore, everyone agrees that financial management is crucial for commercial endeavors.

Concept of Financial Management

In order to accomplish the goals of a corporate company, financial management is the methodical planning, arranging, directing, and managing of financial resources. In order to increase profitability and guarantee long-term sustainability, it mainly concentrates on making sure that sufficient funds are available when needed and are used effectively.

Estimating capital requirements is one of the core components of financial management. This entails evaluating working capital, which is needed for daily operations like buying raw materials, paying employees, and covering other operational costs, as well as fixed capital, which is needed to buy land, machinery, and equipment. Both undercapitalization and overcapitalization can be prevented with accurate estimation.

The collection of funds is the next crucial task. Money can be raised from external sources like bank loans, financial institutions, and trade credit, or from internal sources like owner's capital and retained revenues. Maintaining financial stability and lowering risk requires selecting the right ratio of debt to equity. The distribution of monies is another essential role. The raised money is invested in successful and fruitful ventures thanks to sound financial management. Resource waste is avoided and revenues are increased through proper allocation.

Credit and cash management are equally crucial. Sustaining sufficient liquidity facilitates short-term obligations and guarantees seamless business operations. Additionally, effective credit management enhances cash flow and reduces bad debts. Lastly, financial control and performance evaluation entail keeping an eye on financial activity using financial statements, ratio analysis, and budgeting tools. These resources support performance evaluation and, when required, remedial action.

Functions of financial management

There is no standard procedure for the financial management role. Depending on the company's size, industry, and customs, the functions differ from one company to another. While financial professionals may be concerned about budgetary administration in medium-sized organizations, the owner of small businesses often manages all matters, including the acquisition and utilization of assets. The money-related directors are given crucial importance in a big enterprise to make decisions on various aspects, such as profit strategy, renegotiating developing obligations, presenting another item, and managing the association's working capital. As a result, depending on the situation, financial management functions differ from company to company. The management of the company's current resources, such as cash, debt claims, and inventories, or the acquisition of assets is typically the focus of business finance research. However, in the innovative approach, account capacity plays a significant role in the general management of the business and does a noteworthy job in organizing and estimating the association's need for assets in order to raise the necessary funds and then putting the acquired funds to good use. Therefore, the three fundamental functions of finance are measuring, acquiring, and using funds.

Importance of Financial Management in Small Scale Industries

To identify small businesses to operate well and be sustainable over the long term, financial management is essential. These businesses typically have limited financial resources; therefore effective planning and money management are crucial to their survival and expansion.

The fact that financial management guarantees sufficient capital is one of its main benefits. It aids in precisely estimating working capital needs, such as raw materials, salaries, and other operating costs, as well as fixed capital needs, such as investments in equipment and machinery. Undercapitalization, which could cause operational disruptions, and overcapitalization, which could result in idle cash, is avoided with accurate assessment. Liquidity is also preserved by financial management. Small businesses have immediate responsibilities, such as paying utility providers, suppliers, and employees on schedule. By ensuring that there are enough money available for daily operations, effective cash flow management preserves the stability and goodwill of the company.

The fact that it increases profitability is another crucial factor. Financial management reduces waste and wasteful spending by allocating and using cash appropriately. Methods like cost control and budgeting aid in raising returns and enhancing operational effectiveness. It lowers financial risk as well. Financial management lessens the burden of high interest payments and lowers the likelihood of financial trouble by keeping debt and equity in a healthy balance. Effective financial planning protects the business from unforeseen losses.

Micro, Small and Medium Enterprises Development Act (MSMED), 2006

The Government of India (Allocation of Business) Rules, 1961 has been amended by the President's order of the "Miniaturized scale, Small and Medium Enterprises Development (MSMED) Act 2006," which was issued through a notification dated May 9, 2007. This correction states that the Ministry of Small Scale Industries and the Ministry of Agro and Rural Industries have combined into a single ministry, "Service of Micro, Small and Medium Enterprises." The business assigned to the Ministry of Micro, Small, and Medium Enterprises is listed in the Second Schedule of the Government of India (Allocation of Business) Rules 1961.

The MSMED Act of 2006, which recognized the concept of "large business" and included both assembling and administrative divisions in addition to defining the medium-sized businesses under the MSME section, significantly increased the MSME area's scope and inclusion. The whole non-farming sector of the Indian economy has now been included in the MSME division, according to the revised standards approved for defining MSMEs, separately for the assembly and administration segments.

Table 1: Investment Limit of MSMEs

Classification	Manufacturing Enterprise	Service Enterprise
Micro	Upto 25,00,000	Upto 10,00,000
Small	25,00,001 upto 5,00,00,000	10,00,001 upto 2,00,00,000
Medium	5,00,00,001 upto 10,00,00,000	2,00,00,001 upto 5,00,00,000

Source: MSME Development Act, 2006

The Government of India's Ministry of MSMEs has been in charge of organizing the MSME sector. Through its field associations and affiliated workplaces, it develops and implements programs and initiatives for the growth and development of the MSME sector. The Development Commissioner (MSMEs) has been employed by the Ministry of MSMEs as the nodal Development Agency. It has been the leading organization in promoting, assisting, and identifying strategies and initiatives for the

development and progress of the MSME sector. Along with other money-related organizations, the workplace has also been maintaining communication with Central Ministries and other departments or associations of the Central or State Government. In this sense, business, speculation, and development have been aided by the Government of India's strategic initiatives, such as the MSMED Act, 2006 order, the pruning of the saved SSI list, and the encouragement of financial institutions to extend their credit progression to the SME sector.

After passing both chambers of Parliament, the Micro, Small, and Medium Enterprises Development Bill 2005 received the president's approval on June 16, 2006. The Micro, Small and Medium Enterprises Development Act, 2006 (27 of 2006) has been incorporated into the Statute Book and will take effect on October 2, 2006. Requests from the many SME associations across the country as well as a few master advisory committees led to the Bill's approval. The Administrative Staff College of India (ASCI) was tasked by the Indian government to conduct a thorough investigation into the problems and advocate for a fundamental law for small business. The Abid Hussain Committee had previously suggested such a fundamental law. The ASCI's study, which was released in January 2001, has now been thoroughly examined at several levels. A National Focus Group has since been established to assess this comprehensive study, which is divided into three volumes.

Providing measures for the prompt and seamless supply of finance to SMEs and reducing illness among them has been one of the Act's main goals. In the past, industrial units in India were broadly categorized as small and big size enterprises based on the investment ceiling on the existing plants and machinery. There have been several subcategories within the small-scale sector, including women's enterprises, tiny units, ancillary units, and small-scale services and commercial units. In India, the medium-scale units have never been defined before. But since the MSMED Act of 2006 was passed, Indian businesses have been essentially divided into four categories: micro, small, medium, and big. The Government of India has made the growth of the MSME sector a top priority. According to the Ministry of MSMEs' Results Framework Document (RFD) for 2012–2013, the government's mission has been to: In collaboration with relevant Ministries or Departments, State Governments, and other stakeholders, foster the growth and development of globally competitive Micro, Small, and Medium Enterprises, including Khadi, Village, and Coir Industries. Support current businesses; encourage the establishment of new ones; work toward a cumulative increase of 40 to 50 percent in the number of registered businesses; and increase this sector's GDP contribution from the current 8 to 10 percent by the end of the 12th plan period.

Financial Control and Performance Evaluation

For the purpose of to guarantee that resources are used effectively and that organizational goals are met, financial control is a crucial component of financial management. Appropriate control methods are required in small-scale enterprises with limited financial resources in order to prevent waste, poor management, and unstable finances. Comparing actual performance to anticipated performance and implementing remedial action when variances occur are key components of financial control.

Ratio analysis is one of the key instruments in financial control. A company's financial health can be assessed with the use of ratios like liquidity, profitability, and solvency. They shed light on long-term financial stability, operational effectiveness, and the capacity to fulfill immediate obligations. Another useful method is break-even analysis. It establishes the sales threshold at which total revenue and total expense are equal and there is no profit or loss. This study aids in pricing and production decisions and helps management understand the minimum output needed to prevent losses. The income statement, often known as the profit and loss statement, displays the business's operational outcomes over a given



time frame. It allows management to evaluate overall profitability and cost control by highlighting revenue, expenses, and net profit or loss.

Analysis of the balance sheet gives details on the company's financial situation at a specific moment in time. It aids in assessing solvency and capital structure by displaying assets, liabilities, and owner's equity. The cash flow statement keeps track of the money coming in and going out, making sure the company has enough cash on hand to pay its debts. By using these tools to conduct regular financial reviews, one can find deviations from intended performance and take prompt remedial action, which enhances financial stability, profitability, and efficiency.

Financial Problems of Small Scale Industries

Though small-scale industries (SSIs) are important for economic growth and job creation, they suffer a number of financial issues that have an impact on their sustainability and performance. These businesses frequently struggle to maintain financial stability because of a lack of resources and managerial restrictions. Inadequate working capital is one of the main issues. Many small businesses lack the money necessary to cover regular operating costs like buying supplies, paying employees, and paying energy bills. This scarcity lowers operating efficiency and throws off production cycles.

The high cost of borrowing is another significant problem. Small businesses frequently rely on outside funding sources like banks or private lenders. However, individuals can be subject to higher interest rates because of their inadequate credit history and lack of collateral security. Profit margins are lowered and the financial burden is increased.

Another frequent issue is consumer payment delays. The cash flow of small businesses is negatively impacted when buyers delay payments. They may have to borrow more money to cover regular expenses as a result of these liquidity issues. Poor record-keeping techniques are a problem for many small industries. Accurately evaluating financial performance is challenging due to inadequate accounting systems and poor record-keeping practices. Additionally, this restricts their capacity to obtain institutional loans.

Another significant barrier is a lack of financial knowledge. Owners frequently make financial decisions without expert advice, which results in poor planning and ineffective use of funds. Furthermore, small businesses have less access to long-term funding for modernization and growth. Because of the perceived risks, financial institutions could be reluctant to offer long-term loans. When taken as a whole, these financial issues lead to low profitability, inefficient operations, and a high failure rate for small businesses.

Measures to Improve Financial Management

For Small Scale Industries (SSIs) to become more efficient, profitable, and sustainable, financial management must be improved. Adopting methodical procedures can greatly boost these businesses' financial condition, as financial constraints are a big obstacle. Adopting appropriate accounting systems is one crucial step. Tracking income, expenses, assets, and liabilities is made easier by keeping up-to-date and accurate financial records. An organized accounting system increases credibility with financial institutions, promotes informed decision-making, and increases transparency.

Regular budgeting and financial planning is another crucial stage. Entrepreneurs can predict future financial demands and allocate resources effectively by creating budgets for sales, production, cash flow, and capital spending. Comparing actual performance to planned targets and taking appropriate



remedial action when needed are further benefits of budgetary control. To keep liquidity, better cash flow monitoring is essential. SSIs should periodically assess their cash inflows and outflows to make sure they have enough money on hand to cover short-term commitments and operating costs. Maintaining efficient business operations can be facilitated by timely supplier payments and effective receivables management.

Online banking, digital payment systems, and accounting software are examples of digital financial instruments that can be used to increase productivity and decrease errors. Digitalization facilitates quicker financial transactions, enhances financial reporting, and makes record-keeping easier. It is also critical to support financial literacy and training initiatives for business owners. Business owners who receive training in topics like credit management, investment choices, and cost control are better prepared to handle their finances.

Financial Management Practices in SSIs

In order Small Scale Industries (SSIs) to operate effectively and sustainably, financial management techniques are crucial. The assessment of capital requirements is a crucial procedure that entails figuring out the working capital needed for daily operations, such as wages, raw materials, and other costs, as well as the fixed capital required for assets like machinery, equipment, and land. Precise estimation guarantees seamless operations and avoids financial deficits or unused funds.

The procurement of finances is another crucial procedure. SSIs obtain funding from both external and internal sources, including trade credit, banks, and financial institutions, as well as from internal source such the owner's capital and retained earnings. Selecting the appropriate mix of funds reduces the cost of capital while preserving financial stability. Fund allocation is also essential since it guarantees that resources are employed effectively for profitable endeavors, preventing waste. Maintaining liquidity through efficient cash, inventory, and receivables management is the core goal of working capital management. Effective working capital management guarantees that the company can fulfill its immediate obligations and run smoothly.

Challenges in Financial Management

The performance and sustainability of small-scale industries (SSIs) are greatly impacted by a number of financial management issues. One of the most prevalent problems is a lack of working capital, which makes it difficult to do daily tasks like buying supplies, paying employees, and paying other operating costs. Business continuity and production delays might result from a lack of operating capital. The high cost of borrowing is another problem. Due to a lack of collateral or a poor credit history, small businesses that frequently depend on outside funding from banks or private lenders may pay higher interest rates. This lowers overall profitability and adds to the financial strain.

Cash flow issues are made worse by clients' late payments. SSIs may find it difficult to fulfill short-term obligations when receivables are not collected on schedule, necessitating expensive borrowing. Other significant limitations include inadequate record-keeping and a lack of financial knowledge. Financial discipline is weakened and informed decision-making is hampered by the fact that many small business owners do not keep accurate accounting records or possess sufficient understanding of financial planning and control.

Conclusion

A crucial factor in determining the sustainability and success of small-scale industries (SSIs) is financial management. Effective planning, allocation, and control of cash are crucial for attaining stability and

growth because small businesses have limited financial resources. SSIs can meet short-term obligations, preserve sufficient cash, and guarantee seamless daily operations by implementing sound financial management procedures. Simultaneously, sound financial planning reduces the dangers of excessive borrowing, bad investment choices, and cash flow irregularities. Small businesses encounter many financial obstacles, including insufficient working capital, restricted access to institutional financing, and a lack of financial knowledge, despite their substantial contribution to economic growth and job creation. These difficulties frequently prevent them from growing and lower their overall profitability. However, SSIs can enhance operational effectiveness and financial performance by implementing systematic financial management techniques, such as appropriate accounting systems, budgeting, cash flow monitoring, and financial analysis.

Additionally, government programs and financial institution help can improve access to reasonably priced credit and lessen financial stress. Therefore, in a dynamic economic climate, ensuring the long-term viability, competitiveness, and expansion of small-scale enterprises requires strengthening financial discipline and expanding access to financing. A key component of both financial and non-economic activities, financial management encourages the selection of efficient account acquisition and utilization. Historically, the field of financial management was a branch of bookkeeping using traditional methods. Today, with the influence of industrialization, it has been created with multifaceted and inventive capacities in the business sphere. They are making more progress in the subject of financial management, which has become a vital component of corporate concerns. Corporate funds, business funds, monetary financial aspects, money-related science, and financial engineering are other names for financial management. Comprehending the core concept of financial management becomes essential for those studying finance, business, and the board.

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