

DEFENCE INDUSTRY



SECTOR OVERVIEW

The Defence Industry of India is an important Sector in India, with strength of over 1.3 Million active personnel. India has the third largest armed forces in the world with world's largest volunteer army and one of the largest importers of Defence equipment.

The budget 2016- 2017 includes a capital outlay of Rs 86,488 Crore for new equipment, weapons, aircraft, naval warships, Army vehicles.

India has been spending nearly USD 3.5 billion to boost its military equipment. It has been pushing for greater indigenisation of the military industry as India imports around 70 per cent of its Defence hardware mainly from Russia, Japan, Israel and United States.

STATISTICS

- The allocation for 2016- 17 Defence budget has increased by 9.76% to Rs 2.58 Lakh Crore as compared to the revised estimates of Rs 2.33 Lakh Crore for 2015-16 even as military pension zoomed to Rs 82,000 Crore mainly due to the One Rank One Pension scheme. The capital outlay for the three services (Indian Military, Indian Air Force and Indian Naval services), for modernisation, stood at Rs 78,586.68 Crore. The Defence budget accounted for nearly 17.2 per cent of the total Central Government expenditure for the year 2016-17 which is Rs 19.78 Lakh Crore.

- India is one of the largest importers of conventional Defence equipment and spends about 31.1% of its total Defence budget on capital acquisitions. About 60% of its Defence requirements are met through imports.

REASONS TO INVEST

- The opening of the Defence Sector for private Sector participation will help foreign original equipment manufacturers to enter into strategic partnerships with Indian companies and leverage the domestic markets as well as aim at global markets. Besides helping in building domestic capabilities, this will also bolster exports in the long term.
- The Offset Policy 2016 (which stipulates the mandatory offset requirement of a minimum 30% for procurement of Defence equipment in excess of USD 306.69 Million) introduced in the capital purchase agreements with foreign Defence players. It would also ensure that an eco-system of suppliers is built domestically. Contractual offset obligations worth approximately USD 4.53 billion in next 5-6 years.
- India has modernisation plans with an increased focus on homeland security and India's growing attractiveness as a Defence sourcing hub.
- Prime Minister Narendra Modi's plans to transform India, from its current position as the world's largest importer of military equipment into a manufacturing powerhouse as the country's Defence spending is expected to swell to 620 Billion (Rs38 Lakh Crore) by 2022.
- The Indian private Sector is also scouting for foreign partners with USD 130 billion of military contracts up for grabs in the next few years. The Reliance Group in 2016 acquired Pipavav Defence and Offshore Engineering, making its foray into the Defence Sector, driven by the Narendra Modi Government's 'Make in India and 'Skill India initiatives'.

SECTOR POLICY

Procurement Policy:

- The Defence procurement is governed by the Defence Procurement Procedure (DPP 2016). Latest revision of DPP was released in March 2016.

Offset Policy:

- The key objective of the Defence Offset Policy 2016 is to leverage capital acquisitions to develop the domestic Defence Industry. Mandatory offset requirements of a minimum of 30% for procurement of Defence equipment in excess of USD 307.69 Million have been envisaged.

Procedures for the Grant of Industrial Licenses have been streamlined:

- Guidelines for the extension of validity of industrial licenses have been issued. The initial validity period of industrial licenses has been increased from 3 years to 15 years with a provision to grant extension for a period of 3 years.

MAJOR PLAYERS

Between January 2001 and February 2016, the Ministry of Commerce had granted 333 industrial licences to private firms for Defence manufacturing, according to data on the department of industrial policy and promotion (DIPP) website which includes Micronel Global Engineers Pvt. Ltd, Marine Electrical (I) Pvt. Ltd, Defsys Solutions Pvt. Ltd, Naistoco India Pvt. Ltd, Comint Systems and Solutions Pvt. Ltd., Ananth Technologies Ltd, DCX Cable Assemblies Pvt. Ltd and OIS Advanced Technology Pvt. Ltd. Other industries are Tebma Shipyards Ltd, Premier Explosives Ltd, Titagarh Wagons Ltd, Taneja Aerospace and Aviation Ltd, Punj Lloyd Aviation Ltd, Dynamatic Technologies Ltd, Bharati Shipyard Ltd, Ashok Leyland Defence Systems Ltd and AMW Motors Ltd.

STATE RUN

Name of the Organisation	Specialization	Revenue
Bharat Electronis	Avionics	Rs. 70.93 billion (USD 1.1 Million)
Bharat Earth Movers	Transport	Rs 28.02 billion (USD 430 Million)
Bharat Dynamics	Ammunition and Missile systems	Rs. 32.82 billion (USD 510 Million)
Defence Research and Development Organisation	Research and Development	Rs. 103 billion (USD 1.6 billion)
Garden Reach Shipbuilders and Engineers	Naval ships	Rs 16.94 billion (USD 260 Million)
Goa Shipyard	Shipyard	Rs 6.81 billion (USD 110 Million)
Hindustan Aeronautics Limited	Aerospace manufacturer	Rs 177.53 billion (USD 2.7 billion)
Mazagon Dock Limited	Shipbuilding	–
Mishra Dhatu Nigam	Metallurgy	–
Ordnance Factories Board	Defence Equipment and Support	Rs 162.46 billion (USD 2.5 billion)

PRIVATE PLAYERS

- Tata Group
- Mahindra Group
- Hero Group
- Reliance Industries
- Reliance Anil Dhirubhai Ambani Group
- Bharat Forge
- Hinduja Group
- Larsen and Toubro (L&T)
- Adnani Defence System and Technologies Limited

MAJOR DEVELOPMENTS AND INVESTMENTS



- A Memorandum of Understanding (MoU) has been signed between India and South Korea for Defence Industry cooperation in shipbuilding. Under the MoU, the two countries would recommend the organisations for collaborating in the implementation of specific projects. The MoUs signed will be valid for a time period of 5 years and are automatically extendable for further successive five years at a time. While South Korea is yet to name its recommended organisation, India has nominated Hindustan Shipyard Ltd (HSL), Visakhapatnam for the collaboration.
- Kangnam Corporation of South Korea is slated to provide consultancy, design and technological assistance to India's state-owned Goa Shipyard Limited in building 12 mine countermeasures vessels.
- India and Israel have inked Defence deals worth over USD 2 billion for advanced medium-range surface-to-air missile (MRSAM) systems. As part of the deal, Israel Aerospace Industries (IAI) will provide the Indian Army with Barak-8 advanced MRSAM systems. MRSAM is an advanced ground breaking air and missile Defence system that can provide ultimate protection against a variety of aerial threats such as hostile aircraft, missiles and drones. It has been developed jointly by IAI and India's Defence Research and Development Organisation (DRDO). Other firms involved in project include Rafael, Bharat Electronics Limited, Bharat Dynamics Limited and L&T.
- The Defence Acquisition Council (DAC) of the Union Defence Ministry has approved proposal to procure fresh batch of Barak surface-to-air missiles (SAM) for the Indian Navy's warships from Israel. The procurement of the missiles will enhance India's maritime capability in view of the changing security dynamics in the Indian Ocean region (IOR). The missiles will be procured under 'Buy Global' category from Israel's Rafael Advance Defence Systems Limited at an approximate cost of around Rs 500 Crore. Israeli-built Barak short-range SAMs are installed on most of the front-line warships of the India Navy, including the aircraft carrier INS Vikramaditya.
- The Indian Navy has unveiled the Integrated Automatic Aviation Meteorological System (IAAMS) at Rajali Air Station in Tamil Nadu. The aim of IAAMS is to modernise the meteorological infrastructure of the nine Naval Air Stations (NAS). It is

expected to bring accuracy in weather monitoring mechanism in the Indian Navy. AAMS is equipped with the state-of-the-art meteorological sensors viz., Radar Vertical Wind Profiler, Ceilometer, Transmissometer and Automatic Weather Observation System. It undertakes automatic and continuous recording of relevant weather parameters that are vital for accurate weather forecasting. Installation of the system at remaining eight stations is expected to be completed by March 2019. After completion, the project will give a major fillip to aviation safety, through automation of weather monitoring process.

- Indian Navy has commissioned latest indigenously developed surveillance ship INLCU L51. It was commissioned at a ceremony held in Port Blair, Andaman and Nicobar Command of Navy
- The Indian Navy has de-inducted TU142M Long Range Maritime Patrol aircraft after 29 years of dedicated service to the nation and 30,000 hours of accident-free flying. Now its role will be taken on by the newly inducted Boeing P-8I aircraft.
- Russia has agreed to manufacture in India 200 Kamov KA 226T helicopters with HAL as the Indian pivot. Another 200 helicopters could follow.
- The major naval assets already ordered or in the pipeline include both sub-surface and surface ships. Indian submarine plans formulated in 1999, cleared the acquisition of 24 submarines over a period of 30 years. Out of these, six were to be Scorpene class, already in service with the navy. The project, being executed by the Mazagaon Docks, is behind schedule by four years. The first of these joined the fleet in 2016. All six should be with the navy by 2020.
- In terms of surface ships, the Mazagon Docks and Garden Reach Shipbuilders and Engineers have orders for six stealth frigates. The collaborating foreign partner is Fincantieri, Italian Shipbuilding Company. Three Kolkata class and four Destroyers, a part of Project 17B, are amongst the other ongoing ones.
- The Defence Research and Development Organisation (DRDO) has handed over three naval systems to the Indian Navy. These latest systems will significantly enhance the navy's navigation and communication network.
- So far 124 ultra light howitzers are to be procured from the US. The DRDO has produced the Dhanush 155mm 45 calibre towed gun based on the designs of the Swedish Bofors. For the tracked version, apparently the army has opted for the K9 Howitzer developed by L&T-Samsung
- The basic tank that we have is the Russian origin T90s, a third generation Russian origin platform. By 2020 India should be able to field up to 40 tank regiments equipped with the T90. The rest of our tanks are primarily the older T-72. These are being upgraded with better night vision devices. Orders have been placed for 124 Arjun tanks. The Arjun Mk II is being progressed with 70 modifications to be incorporated.
- The USD 2.5 billion Kalyani Group, of which Bharat Forge is the flagship company, announced a partnership with Israel's Rafael on Feb. 19, will make Spike anti-tank guided missiles for the Indian armed forces.

- India and Russia have signed two long-term support agreements for the Sukhoi Su-30MKI combat aircraft fleet, covering around 57,000 spares and components related to the aircraft.



INVESTMENT OPPORTUNITIES

1. Defence products manufacturing.
2. Supply chain sourcing opportunity.

FOREIGN DIRECT INVESTMENT POLICY

- 100% Foreign Direct Investment (FDI) in Defence Sector: Up to 49% under automatic route; FDI above 49%, through Government route.

GOVERNMENT INITIATIVES



- The Narendra Modi Government in its first year cleared 39 capital procurement proposals, of which 32 proposals worth 889 billion (USD 14 billion) (or 96% of value of total proposals) were categorized as *Buy (Indian)* and *Buy and Make (Indian)*—the top two prioritized domestic industry-centric procurement categories as per the Defence procurement procedure (DPP).

- In July 2015, the Defence Ministry eased export regulations and stopped demanding multiple assurances on end-use from foreign Governments even for sale of components by Indian entities.
- There are several Indian SMEs that cater to the Defence industry by supplying sub-assemblies and components and providing services like system integration. Under the Make in India initiative, these organizations are set to enhance their manufacturing and development efficiency, thereby contributing to making India self-reliant in Defence production. Some of the system Integrators catering to the Defence Sector in India are Mistral Solutions, Alpha Designs, Astra Microwave and SLN Technologies among others.

FOREIGN INVESTORS

Airbus (France)BAE India Systems (UK)Pilatus (Switzerland)Lockheed Martin (USA)Boeing India (USA)Raytheon (USA)Israel Aerospace Industries (Israel)Rafael Advanced Defense Systems Ltd. (Israel)Dassault Aviation SA (France)



AGENCIES INVOLVED

- Ministry of Defence, Government of India
- Department of Defence Production, Ministry of Defence
- Department of Industrial Policy and Promotion, Ministry of Commerce and Industry, Government of India
- Department of Commerce, Ministry of Commerce and Industry, Government of India
- Defence and Strategic Industries Association of India

GROWTH

Defence Production Policy, 2011 has encouraged indigenous manufacturing of Defence equipment. Defence Procurement Procedure (DPP) has been amended in 2016 to provide for the following:

1. New category of capital procurement - Buy Indian —IDDM (Indigenously Designed, Developed and Manufactured) introduced to encourage indigenous design, development and manufacturing of Defence equipment.
2. Provisions to allow foreign OEM (Original Equipment Manufacturer) to select Indian Production agency.
3. The Defence security manual for the private Defence Sector manufacturing units has been finalized and put in public domain by the Department of Defence Production. The manual clarifies the security architecture required to be put in place by the industry while undertaking sensitive Defence equipment.
4. The MAKE procedure, which aims to promote Research and Development in the industry with support from the Government and the placement of orders, has been promulgated with provision for 90% funding by Government and preference to Micro, Small, and Medium Enterprises (MSMEs) in certain category of projects.

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