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## Companies cheer defence purchase policy changes, but analysts cautious

With design and development being done by Indian firms, quality of products will meet the armed forces' tough evaluation process, say experts

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P.R. Sanjai



Photo: Bloomberg

Indian defence companies said on Tuesday that they are excited about new business opportunities, a day after the defence ministry approved policy changes to give priority to locally made defence equipment. But experts were cautious about the stringent conditions imposed by the ministry.

The Defence Acquisition Council (DAC), the apex decision-making body of the ministry, on Monday approved changes to its Defence Procurement Procedures (DPP) to introduce a new category for indigenously made products.

Under the new category for Indigenously Designed, Developed and Manufactured (IDDM) equipment, it will be mandatory for 40% of the content to be sourced locally.

“The new category of IDDM equipment is ingenious. This changes everything. The impact will be far-reaching and will have a cascading effect,” said Ashok Atluri, managing director, Zen Technologies Ltd, which designs and manufactures training simulators.

“This will change India from being a destination for low-cost manufacturing to being a starting place for cutting-edge

innovation, and from being a consumer of out-dated equipment to being a producer of trailblazing technology, as also from being the world's largest importer to being a leader in export of defence equipment," Atluri said.

For more than a decade, the government has tried to rope in the private sector for defence production. But domestic manufacturing is still dominated by the defence public sector enterprises and the Ordnance Factories Board, which together have an 80-90% share.

Local manufacture of defence equipment is at the heart of the government's Make in India programme too, but the country continues to import nearly 60% of its defence equipment.

Another addition to the DPP is a policy to fund Indian private entities in research and development in order to encourage more local development, resulting in micro, small and medium enterprises (MSMEs) getting more opportunities.

Atluri said that with design and development being done by Indian companies, the quality of the products will meet the tough evaluation process of the Indian armed forces. This will ensure that India not only becomes self-reliant but also exports defence equipment.

"Additionally this is a ground-breaking policy which will benefit the micro, small and medium enterprises enormously. First, the Buy Indian (IDDM) category will attract a lot of SMEs to develop products that are required by the Indian armed forces and as it will have the top-most priority it will invigorate the SMEs significantly," Atluri said.

He also said that under the 'Make' category, government-funded projects worth less than Rs.10 crore will be reserved for SMEs. The Make-III category is for the MSMEs, and will be reserved for projects worth less than Rs.3 crore.

"Also, the assurance of orders has been given. And if the order is not placed within 24 months of development, the development cost will be refunded," Atluri added.

Puneet Kaura, managing director and chief executive officer at Samtel Avionics Ltd, said the proposed changes show the government has firmly focused on developing indigenous manufacturers, especially MSMEs.

Experts, too, are convinced about the broader objectives of the policy changes brought in by the defence ministry.

"Defence procurement must fulfil four key criteria: quality of equipment purchased so our forces get the best, cost-effectiveness, transparency and indigenization. The changes proposed in the DPP are largely positive and do address these issues", said Dhiraj Mathur, partner and leader (national aerospace and defence practice) at consultancy firm PwC.

However, Mathur was sceptical about the offset opportunities.

Offsets, currently, are a provision in the DPP that require any foreign arms manufacturer securing an order worth more than Rs.300 crore from India to source components worth 30% of the value of the order from India.

The DAC has revised the so-called defence offset clause, which will now be applied to contracts of more than Rs.2,000 crore instead of the current Rs.300 crore, thereby removing a hurdle for foreign companies eyeing the Indian market.

"The IDDM and the proposed 'strategic partnership' are both very good ideas to promote indigenization and bring in greater transparency. However, raising the threshold of offset requirements to Rs.2,000 crore from current Rs.300 crore is counter-intuitive. On the one hand, the government wants to promote local manufacturing and the other you are increasing the limit of offset requirements," Mathur said.

Another defence consultant, requesting anonymity, said the proposed changes suggest the government will release more orders to procure defence equipment shortly.

"The changes are imposing more conditions on the foreign capital. The government is insisting on transfer of technology up to 90% while encouraging local production. One will have to wait and watch how the capital is flowing to the country with such stringent conditions," he added.

 **P.R. Sanjai**

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