

## DPP 2016: A Game Changer For Indian Defence Industry

*The most revolutionary aspect of the new Defence Procurement Policy (DPP) is the introduction of the new category called Buy Indian - Indigenously Designed, Developed and Manufactured (IDDM)*



**21** January, 2016  
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This is a game changing policy which will push India towards rapid indigenisation and on the path to self-reliance and global leadership in defence. While the key provisions of the policy were announced after repeated delays, the final outcome is indicative of the enormous efforts that more than justify the delays.

### Buy Indian

The most revolutionary aspect of the new DPP is the introduction of the new category called Buy Indian-Indigenously Designed, Developed and Manufactured (IDDM). For the first time in the history of Indian defence procurement the importance of design and development has been recognised by the Ministry of Defence. It is important to state that only if equipment is indigenously designed and developed will there be more jobs employing scientific talent and India, from being the largest importer, will become a global leader in defence equipment. The game is that the technology, the IP in the products, should be owned by Indian companies. Otherwise we shall be forever dependant on foreign technology and will never become a global leader for the defence industry. Given the fact that almost 70% to 80% of the value capture is done at the design level, it was strange that no provision existed till now to encourage the design and development in India. The focus, till now, has been, at best, on getting the technology and becoming low-cost manufacturing coolies at best, or just, worst, just importing. Introduction of the new category, IDDM, changes everything.

As per Buy Indian (IDDM), if the product is designed in India and 40% of the equipment has indigenous content it will qualify under this category. If 60% of the content is indigenous, and even if the design is not owned by Indian company, this clause will be applied.

This category is going to ensure huge inflow of funds into research and development and will ensure that the scientific talent in India is engaged in developing cutting edge technologies in Defence. With such huge investments, going into R&D, India, far from being a destination for out-dated equipment, will become the source for trail-blazing technology in defence.

### Single vendor situations

Another issue that the Indian industry had was the insistence previously by the Ministry of Defence for having at least two vendors till TEC stage even under Buy Indian category. For much of the defence equipment, there are only 4 or 5 major vendors world-wide, expecting 2 vendors even under Buy Indian category would be foolhardy and this anomaly existed earlier. The new DPP ensures that even if single vendor situation arises at bid stage, the procurement will be concluded, if the product qualifies and due process is followed.

The other changes include increase of indigenous content under Buy Indian category from 30% to 40%. Under Buy and Make Indian and Buy and categories the requirement of indigenous content has been raised from 30% to 50%.

### RFP Parameters - finer distinction

With respect to RFP, on the request of various stakeholders especially the armed forces, the parameters have been divided into three categories 'A', 'B' and Enhanced Performance Parameters.

'A' parameters are those parameters which are to be demonstrated at trial stage itself.

'B' parameters are those parameters which need not be demonstrated during the trial process but the capability to integrate them should be conveyed to the Ministry of Defence and the same should be included in the production units.

Enhanced Performance Parameters is for additional capabilities over and above the essential parameters for which additional credit score will be given to the vendor while evaluating the product cost.

#### **Increase in Offset Threshold - Mystifying**

One mystifying aspect in this policy is the increase in applicability of offset clause for acquisitions from foreign vendors from Rs 300Cr to Rs 2000cr. Three reasons can, probably, be assigned for increasing this limit:

1. The Ministry of Defence possibly found it difficult to properly monitor so many offset proposals and contracts. With Rs 2000 crores, there would be lesser offsets to take care of, thus better monitored.
2. The evaluation of quality offset obligation, under the new dispensation, has become extremely rigorous and any deviations, which were being allowed earlier, are now being rejected. This has led to piling of vast unfulfilled offset obligations.
3. The cost of acquisition becomes significantly high when offset obligation is included. In fact the Ministry of Defence has gone on record and said that the cost quoted by the vendor increases by as much as 20% whenever there is an offset obligation.

Perhaps these reasons could have convinced the Ministry of Defence to increase the offset requirement from Rs 300 crore to Rs 2,000 crore.

#### **Make Procedures**

Another major change that has happened is with respect to make procedures. Make procedure has four sub categories:

1. Government funded projects: Under this category 90% of the funding is done by the government and 10% is industry funded. There are two subcategories under this-
  - Projects under Rs 10 crore are reserved for MSMEs
  - Open category if it is more than 10cr or if MSME cannot develop it even if it is under 10 crore
2. Industry funded projects:
  - Projects under Rs 3 crore are reserved for MSMEs.
  - More than 3 crore it is Open category

#### **Bold Step - Refund of R&D Expenditure if orders not placed**

One encouraging feature for all the make projects where the product development is successful is that if the Government does not place the order within 24 months of developing the product, the government will refund 100% of contribution made by the industry. This increases the Govt's responsibility tremendously and insures the risk taken by the industry.

Again under make only firms with majority controlled by Indian residents will be eligible to participate. In addition the companies should be existence for 5 years (3 in the case of MSMEs) and they should be rated B++. Minimum net worth criteria of 5% has been set in relation to the development cost only in cases where the development cost is exceeding 5,000 crore. Otherwise positive net worth is the minimum eligibility criteria to bid for projects.

Overall this is a great policy initiative that the Indian defence industry and something that the country can cheer about. I believe this policy is the fastest way to the path of self-reliance in Defence.

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