

# THE NEW SPITFIRES

Indian defence SMEs are betting on the new defence procurement policy to boost indigenous manufacturing, but challenges remain  
By Ashish Sinha



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**WAVE** of optimism is sweeping home-grown small and medium enterprises (SMEs) associated with the Indian defence sector. The government's Make in India initiative and particularly its defence offset policy has come as a shot in the arm for a number of SMEs that have gained from the rule requiring global defence suppliers to invest 30 per cent of the equipment deal amount in the Indian market by way of local sourcing. SMEs such as Noida-based Samtel Avionics, Kanpur-based MKU and Bangalore-based SI2 Microsystems, among others, have seen their order books swell as a result.

Now, all eyes are on the much-delayed Defence Procurement Policy 2015 (DPP 2015), which is expected to unleash the next wave of local manufacturing to meet the growing demand of the Indian armed forces.

Take Bangalore-based SI2 Microsystems, for instance. After a subdued couple of years owing to the global slowdown, when demand from the local industry kept it going, the company is now betting on DPP 2015 to change its fortunes. "We expect key projects from Hindustan Aeronautics (HAL) for indigenisation of sub-systems for the MIG and Sukoi aircraft and more projects from MBDA Missile Systems (France) in the missile testing area. Our current order book is nearly Rs 30 crore, but we expect healthy growth over the next two years," says Sanjay Soni, president, SI2

## MFD DISPLAY SYSTEMS

A multi-function display is a small screen used to display information in numerous configurable ways



## MFD FOR LCH

MFD is used in concert with primary flight display and forms an integral component of glass cockpit. After Su-30 fighters, Samtel will now be supplying MFD for the Light Combat Helicopter



Microsystems. Besides, the Indian Space Research Organisation (ISRO), Defence Research and Development Organisation (DRDO), Bharat Electronics (BEL), HAL and the Indian Air Force, SI2 Microsystems also works for MBDA Missile Systems, ELISRA, Stratasys, Sicon Tech (Israel) and Analog Devices (US), among others.

Like SI2 Microsystems, Samtel Avionics too has benefitted from the 30 per cent local sourcing norm. Its managing director and CEO, 37-year old Puneet Kaura, is expecting the order book to swell with the coming of the DPP 2015. "Now much will depend on what kind of emphasis is laid on local sourcing under DPP 2015 and what its fine print is," says Kaura.

For Manoj Gupta, chairman of Kanpur-based MKU, another mid-size defence SME, the strict enforcement of the local sourcing norms for global defence OEMs (original equipment manufacturers) is a "good step" for companies like his and may lead to a level playing

field for SMEs while competing for orders from large defence public sector undertakings.

But unlike SI2 Microsystems, both Samtel and MKU have survived the uncertainty in defence procurement and the inadvertent delays associated with defence offset contracts thanks to orders from global defence manufacturers. Samtel works with global OEMs in the field of aerospace and defence such as Honeywell, Curtiss-Wright and Saab of United States, General Dynamics of Canada and Thales of France.

MKU is registered with NATO and the United Nations as a regular supplier of ballistic protection solutions such as body armour, vests, helmets as well as other solutions for both soldiers as well as armoured vehicles, ships and aircrafts. Besides, it has been a regular supplier to several police and paramilitary forces, the Indian armed forces, and to public and private shipyards for their naval vessels. The company's domain expertise lies in manufacturing and integrating

ballistic protection solutions for 230 forces in over 100 countries. MKU too is sitting pretty with orders worth around Rs 500 crore and expects more work to come its way once DPP 2015 is officially announced.

Samtel Avionics works with the Indian Air Force (IAF) and others through joint ventures such as Samtel HAL Display Systems and Samtel Thales Avionics. It has been supplying specialised multi-functional display (MFD) systems to IAF's 100-plus Sukoi-30 fighter aircraft. An MFD is a display unit that guides all the functions of an aircraft.

### Awaiting Growth

Samtel expects to corner 25 per cent in the Rs 1,000-crore Indian defence electronics market. Its joint venture with French major Thales will be used for upgrading the displays and avionics of Mirage 2000. "We will be closing the financial year (2015-16) with a consolidated turnover of around Rs 200 crore, double that in 2014-15. For 2016-17, we expect a growth of 20-25 per cent or Rs 250-300 crore," says Kaura.

Kaura's calculations are based on growing dependency on electronics and avionics across military disciplines. Currently, around 30 per cent hardware on a



### MAKE IN INDIA

Indian SMEs are capable of making as high-tech a product as the MFD, which is a display unit that guides all the functions of an aircraft

combat aircraft is electronics. Similarly, a large part of electronics systems are being integrated with armed vehicles for the Indian army — a blessing in disguise for local SMEs.

Besides, the call for Make in India in the defence sector will

help defence SMEs bag contracts in newer areas. "We will diversify into infrared search and track, electronic warfare suites where the private sector is allowed to bid now, and electronics on armed vehicles," says Kaura.

Defence minister Manohar Parrikar recently said, "India cannot afford to spend \$20 billion on defence procurement. Therefore, promoting local manufacturing is a must and the country will promote private players."

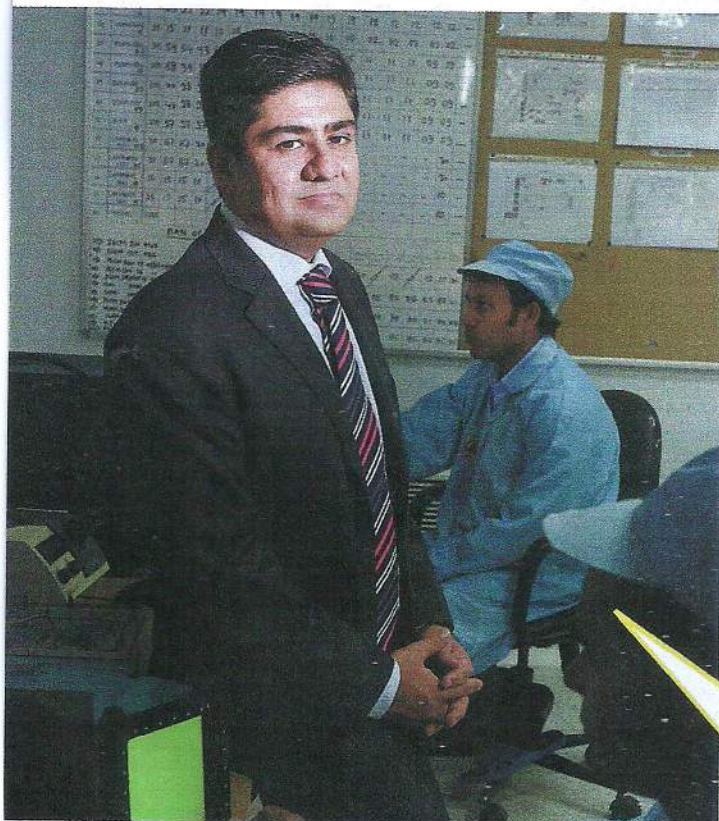
### Healthy Order Book

Samtel Avionics is also sitting on a healthy order book. It will supply MFDs for the Light Combat Helicopter (LCH) through its joint venture, Samtel HAL Display Systems. The multi-role LCH, being developed by HAL is expected to go into production soon. Later, there may be a requirement of around 750 MFDs for LCH. Samtel is also expected to develop products for Tarang, a radar warning receiver developed by the DRDO. It has also supplied three units to BEL for the Tarang programme.

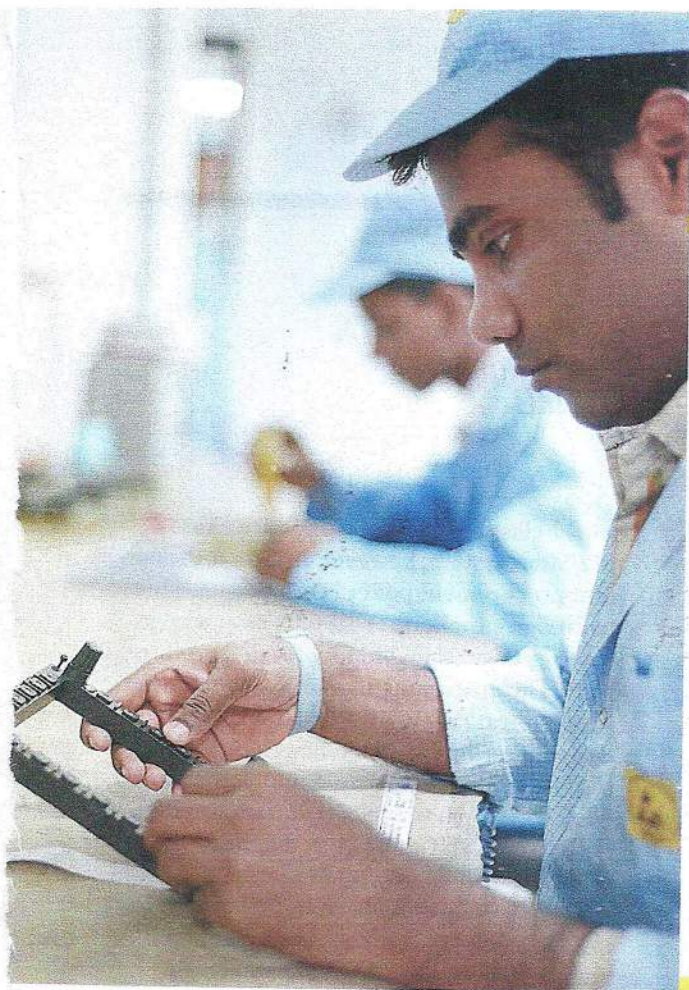
Samtel has also supplied 19-inch rugged displays to BEL for the Battlefield Surveillance System for the

Indian army. "Our order book may close at around Rs 1,000 crore by the end of the current financial year," says Kaura.

Samtel is also banking



**PUNEET KAURA**  
MD & CEO, Samtel  
Avionics



## STEPS TO BOOST LOCAL INDUSTRY

- India is the only major arms importer with low offset requirement
- India's offset policy allows a low 30 per cent offset on a contract threshold of \$55 million
- Other countries demand higher percentage of offsets
- Canada and Malaysia demand 100 per cent offset
- Israel demands offsets on a contract value of \$5 million
- India should consider lowering threshold to \$10 million
- India should raise offset to a minimum of 50 per cent
- India needs to have a dedicated single-window agency to manage offsets
- A single agency should vet offset, award offset credits and monitor them
- India needs to develop a long-term offset policy like Malaysia and Israel
- Provide uniform offset obligation on all players, irrespective of their country
- Allow the local industry to operate in a level-playing field
- Do not discriminate between manufacturing & services

on projects from international joint ventures to take off this year, including those with players such as Honeywell, Curtiss-Wright and General Dynamics, among others. The company has also received a purchase order for Commander Sight Displays on Arjun Main Battle Tank. These displays would be integrated with Arjun MBT Mk II (124 tanks) and the Futuristic Main Battle Tank (124 tanks).

MKU too is sitting pretty, having ended 2014-15 with a turnover of around Rs 247 crore.

"Despite a slowdown, we have been able to maintain our growth trajectory this year. We have a very healthy order book of Rs 350 crore and another Rs 150 crore of projects are in the pipeline. We are confident of growing further in the next two years," says Gupta of MKU.

Instavest', the fastest 'quick release' ballistic jacket produced by MKU is in great demand the world over. It can be divested by the wearer in a single action in a fraction of a second and re-assembled again very quickly, the company claims. MKU's Boltfree Helmet gets exported across the world as it is based on 'no-drill concept' that not only provides uniform protection across the shell but also safety from secondary metallic fragments, the

company says. According to experts, the DPP will allow SMEs access to a wider domestic market unlike at present.

### The Offset Policy

Coming back to the offset norm governing Indian SMEs engaged in indigenous defence production, the policy itself has undergone revision several times since it was announced in 2005. According to the August 2012 policy, 30 per cent offset is mandated in import contracts valued at Rs 300 crore or above. Reports suggest that till December 2014, the defence ministry had signed 25 offset contracts — 16 for the IAF, six for the Navy and three for the Army — valued at \$4.87 billion.

The government now plans to formulate a document for defence manufacturing and procurement with a list of items that are not to be imported starting 2016.

According to industry insiders, DPP 2015 may accept the private sector as main integrators in all major defence projects. But experts point to some red flags in the upcoming DPP 2015 such as capping private firms to one strategic project each or disallowing cross-holdings and expecting indigenisation targets of

# 25%

The share Samtel hopes to corner in Indian defence electronics market



**MANOJ GUPTA**  
Chairman  
MKU

world-class products at competitive rates. SI2 Microsystem, however, feels that the current procurement policy is more favourable to foreign suppliers. "This puts us at a huge disadvantage when bidding for defence projects. The procurement policy has to be modified to create a level-playing field. The armed forces and the defence PSUs have to seriously consider Indian manufacturers and work with them very closely to achieve the objectives of self-reliance in defence requirements," says Soni of SI2 Microsystems.

There are other problems and challenges facing the defence SMEs. These include uncertainty of orders, small batch sizes and high investments in quality management, long certification process and lack of skilled manpower. Experts say the biggest bottleneck for SMEs is the procurement process, which is long, opaque and based on the concept of L1 (lowest cost

60-65 per cent under the 'Buy and Make' (Indian) programme, says Amber Dubey, partner and India head, Aerospace & Defence, KPMG. According to Dubey, the DPP expert panel is made up of retired bureaucrats and military officers with no representation from the private sector. This may pose problems. "For Make in India to happen, we need to abolish state monopolies, support the private sector, and relax the entry of global OEMs," he says.

### Challenges Galore

According to Gupta of MKU, a major challenge for Indian defence SMEs is the government's uncertain procurement policy. "We have been able to overcome it by turning to the international market and not being solely dependent on India. This has enabled us to grow despite the hiccups and establish a global presence. Today, we are present in over 100 countries. This has also helped in driving our R&D and the development of more innovative products and technologies," says Gupta.

Kaura of Samtel believes that a continuity in procurement strategy will help Indian SMEs deliver

wins). Says Dubey, "In this sector, where quality is paramount, L1 cannot be the judging criteria. Moreover, SMEs need support in terms of capital subsidy, tax incentives, interest subsidy, training and infrastructure. A cluster approach with a large OEM as the anchor tenant, and fiscal incentives and focus on skill development would help defence SMEs to become viable and competitive."

For the indigenous defence industry to flourish, Dubey suggests several measures. "Abolish the monopoly of DRDO and the defence PSUs, facilitate the entry of domestic manufacturing industry into defence; increase the FDI limit to 74 per cent to bring cutting edge technology, provide fiscal incentives, set up a fund to support SMEs with easy credit; ease export norms for defence equipment and focus on skill development." Indian

defence SMEs also want the government and the defence PSUs to view SMEs as a national asset and treat them accordingly. Is anyone listening? **BW**

**L1**  
The concept of  
'lowest cost wins' is  
the top bottleneck  
in procurement