

ISAS Brief

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Make in India – Why It Will Succeed¹

Despite the continuing mixed signals about the ease of doing business in India, the author believes that the country will make it to the top echelons of manufacturing hubs in the world.

Girija Pande²

Incredible headlines dot the international business media – India emerges as a competitive Asian manufacturing hub! But when, at the recent Singapore Airshow, two tech giants in the world of defence manufacturing – namely, Russian Helicopters and Lockheed Martin – announced that they were willing to start manufacturing facilities in India, the headlines had to be taken seriously.

“We are ready to manufacture F-16 in India and support the Make in India initiative”, Phil Shaw, chief executive of Lockheed Martin India Private Ltd, told reporters at the recent Singapore Airshow 2016.

Shaw would like to see F-16 roll out of India soon, but awaits government-to-government decision on this strategic project.

¹ This article was first published by *Foreign Investors on India*, a blog, at this link: <http://www.fii-news.com/make-in-india-will-succeed/> on 26 February 2016.

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Lockheed sees India as a low-cost high-quality engineering/manufacturing destination that could lower their cost of production substantially.

It would be a low-cost high-quality model which would assist in selling F-16 planes to India and other emerging markets.

Similarly, Russian Helicopter, which has signed a 200-helicopter contract with the Indian armed forces, is now poised to sign a partnership agreement with Hindustan Aeronautics Ltd within this year to start manufacturing these in India.

Sukhoi Civil Aircraft is also waiting to sign a partnership with Tata Advanced System this year to manufacture airplane parts for its super jet.

The State Advantage

In an otherwise-bleak global outlook, India's US\$ 2-trillion domestic market becomes very attractive, given the long-term growth projections made by the World Bank/International Monetary Fund of 7-8% per annum in the next three years.

Moreover, the Narendra Modi Government in India is rapidly clearing the old cobwebs of laws and regulations by digitizing processes/regulations which had made India one of the most difficult countries to operate in. Following this lead, progressive and pro-business western and southern states in India are racing to clear such regulatory cobwebs to make it easier to do business in their states.

It is such individual states that investors must look to, rather than looking at the whole country, and I believe that this experience will be pleasantly surprising to many.

Despite mixed signals coming out of India's noisy democracy and noisier media, there are four key reasons why, I believe, India will finally make it to the ranks of major manufacturing countries in the world:

1. External influences: China's structural reform of its economy throws up a one-time opportunity to attract low-end manufacturing to India. Higher cost, lower availability of labour due to an ageing populace and the rupee-yuan parity in favour of India are all push factors in this shift of manufacturing from China, particularly southern China. Pull factors would be the size of India's domestic market and cost structures. Members of the Association of Southeast Asian Nations (ASEAN), particularly Vietnam, are better-positioned today than is India. The fact that Vietnam has agreed to sign up to the Trans-Pacific Partnership (TPP) regional trade agreement, which includes giants like the United States and Japan, makes it a very attractive manufacturing base.

2. Pull of the OEM's: All major global Original Equipment Manufacturers (OEM) in the field of auto/white goods/electronic devices are already present in India. This will entail relocation of tier-one and tier-two component-suppliers to plants within India too. They will seek to use India both as a domestic base as well as an export hub for regional markets. Without an exporting capability, India will not attract large-scale manufacturing.

3. Adding capacities to manage growth: After three years of 7% p.a. growth in the Gross Domestic Product (GDP), Indian companies will need to add to capacities, as demand finally overtakes supply. This will happen in consumer goods and infrastructural sectors, creating a favourable cycle of increased manufacturing activities.

4. Private Sector in Defence & Railways expansion: The Government's welcome push in opening up the defence manufacturing industry and the ambitious railways expansion will be a major catalyst for introduction of high-end manufacturing. Global manufacturing giants understand the value of India's talent pool, especially its high-end engineering and software skills, which plays a great part in the new manufacturing paradigm. Moreover, with the dynamic Indian private sector being encouraged to enter the defence manufacturing sector, foreign manufacturers will find excellent Indian counterparts for setting up local subsidiaries.

Asian Manufacturers Contemplating a Move to India

Low-end manufacturers from China who are contemplating a shift out of China will look at India carefully as they see in the rise of India one of the world's largest consumer markets

rivalling that of China. China's electronic manufacturers, too, are attracted to the Indian market, especially mobile telephony and heavy-duty construction equipment markets. Sany, the largest construction equipment manufacturer from China, has ambitious plans for India out of its Pune factory. Foxconn, a well-known electronics assembler, has also started production in India and announced plans to invest US\$ 5 billion. India's plans for Chinese manufacturers include special economic zones which will make it a hub for Chinese-origin but made-in-India products. Benefits of clustering Chinese in such zones are expected to attract Chinese manufacturers in larger numbers. A similar story is seen with Korean and Japanese manufacturing companies. In fact, over the last two decades the Koreans have shown the way by building plants, brands and winning customers in autos, phones and white goods to the surprise of large Japanese manufacturing companies who were sceptical about manufacturing in India some years ago.

India's Challenges and Enablers

India's big challenge remains its woefully inadequate infrastructure and ease of doing business. But this is being tackled, albeit at a slower pace than the "higher anticipation" of investors who expect at least Asian standards. Zeroing in on high-performing Indian states and locating plants in such states is a very viable solution.

Other enablers to attract manufacturing in India is the country's ability to sign up to regional trade deals which allow free cross-border movements in components and become part of the Asian supply chain. India must be bold in this area (as Vietnam did by boldly joining the TPP) because India is traditionally seen as a laggard, subservient to its protectionist domestic lobbies.

Understanding India is important, for it is the world's largest democracy. Though at times it can be annoying to deal with "one billion people with two billion views expressed rather vocally", we must accept that it is these very people whose talent and expertise have led to some incredible headlines.

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