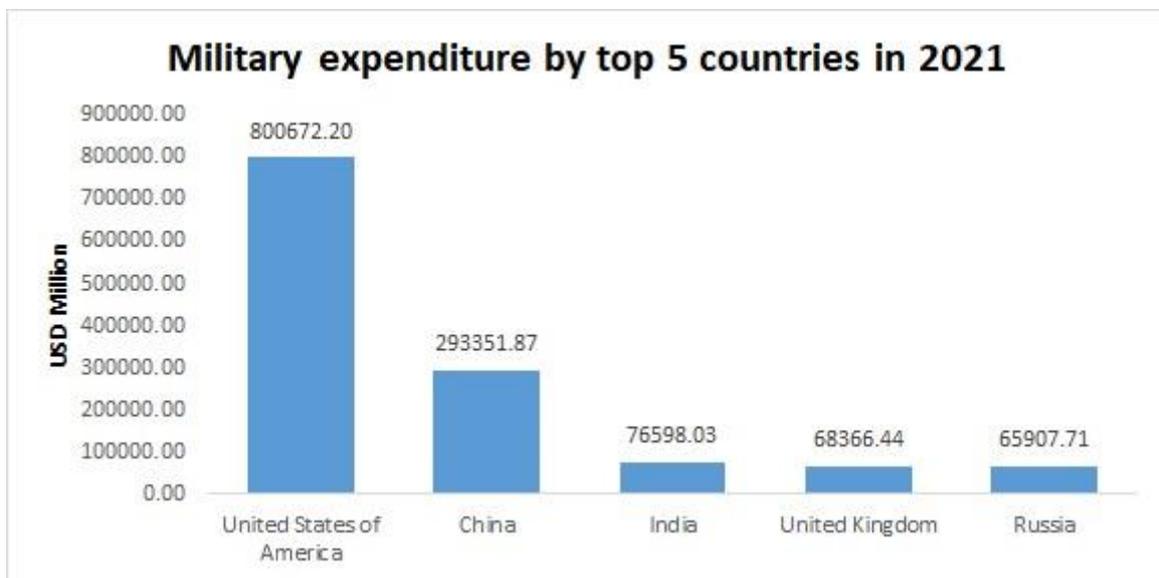


The Indian Defence Sector Analysis

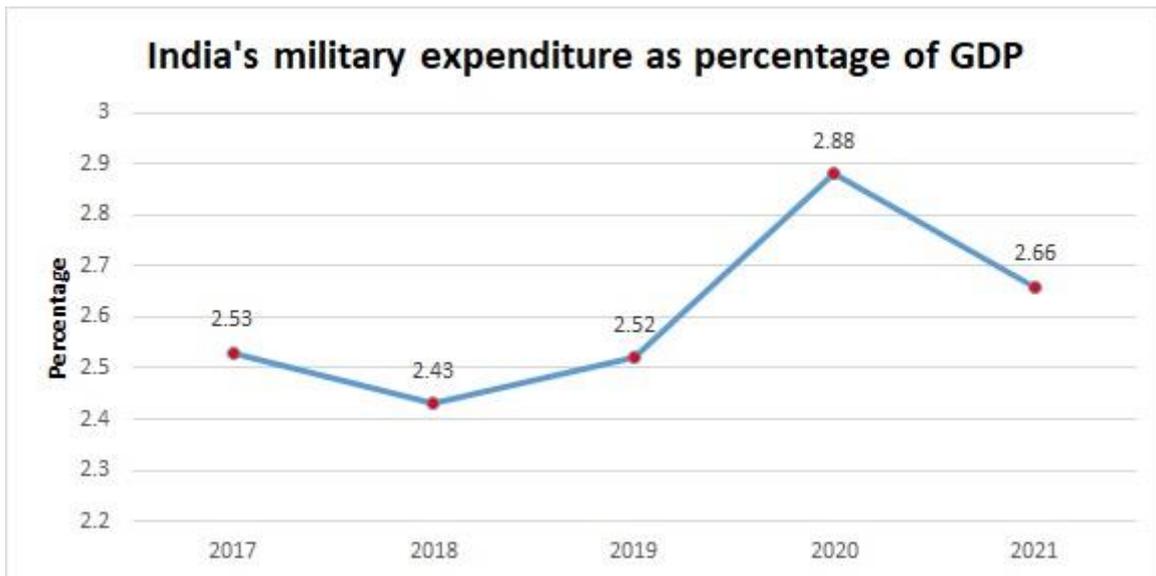
The Indian defence sector over the years has witnessed substantial growth. India has the world's second largest army, fourth largest air force and seventh largest navy. The sector is also open for the Indian private companies. Both, public and private companies along with the government support develop and deliver state-of-the-art defence systems based on the latest indigenously developed technologies. These systems draw on the strength of proven software and hardware architectures and provide safety, security and threat management capabilities to armed forces. The Indian defence manufacturing industry is a significant sector for the economy. The defence manufacturing industry is poised for significant growth considering the increasing security threats faced by India, thereby boosting demand for defence equipment. Incentivised by various government reforms, India is quickly ramping up its manufacturing capacity. It also aims to reduce import dependence. India has one of the largest armies in the world, it is also one of the largest importers of defense equipment which calls for developing robust domestic manufacturing capability.

Military spending by top 5 countries in world

The world's military expenditure reached an all-time high of \$2.1 trillion in 2021. The five largest spenders in 2021 were the United States, China, India, the United Kingdom and Russia, together accounting for 62% of expenditure. India's military spending for the year 2021 has been ranked as third highest in the world. The country's military spending stood at \$76598.03 million. This was up by 0.9% from 2020. In 2021, the US military spending reached \$800672.2 million in 2021, a drop of 1.4% from 2020. Second place went to China, which spent \$293351.9 million on defence, an increase of 4.7% compared with 2020. Meanwhile, United Kingdom military spending stood at \$68366.44 million and Russia spend around \$65907.71 million.

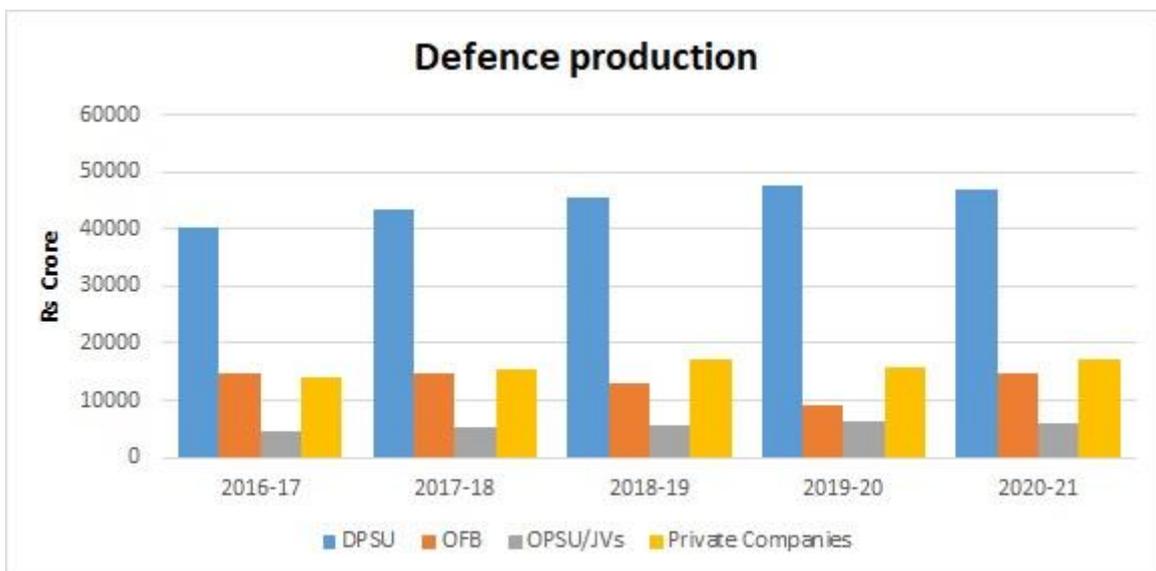


The world military expenditure as a share of world gross domestic product (GDP) fell by 0.1 percentage points, from 2.3% in 2020 to 2.2% in 2021, as a result of a sharp economic recovery in 2021. Russia's military spending reached 4.1% of GDP in 2021. The US military expenditure decreased slightly from 3.7% of GDP in 2020 to 3.5% in 2021. Also, India's military expenditure fell marginally from 2.88% of GDP in 2020 to 2.66% of GDP in 2021. Prior to this, it was 2.52% of GDP in 2019, 2.43% of GDP in 2018 and 2.53% of GDP in 2017.



Defence production

The country's total defence production rose 7.19% to Rs 84760 crore in 2020-21 from Rs 79071 crore in 2019-20. Of the total Rs 84760 crore, defence public sector undertakings (DPSU) contribution is 55.22% with production of Rs 46802 crore in 2020-21, followed by Private Companies (20.40%) Rs 17294 crore, Ordnance Factory Board (OFB) (17.27%) Rs 14635 crore and Other Public Sector Undertakings/ Joint Ventures (OPSU/JVs) (7.11%) produced defence products worth Rs 6029 crore. Earlier, the country's total defence production was Rs 81120 crore in 2018-19, Rs 78820 crore in 2017-18 and Rs 74054 crore in 2016-17. Meanwhile, the Defence Ministry is aiming Rs 1.75 lakh crore of defence production by 2025, which will include export of Rs 35,000 crore. The major role in achieving this goal with a contribution of 70-80% would be done by India's DPSUs.



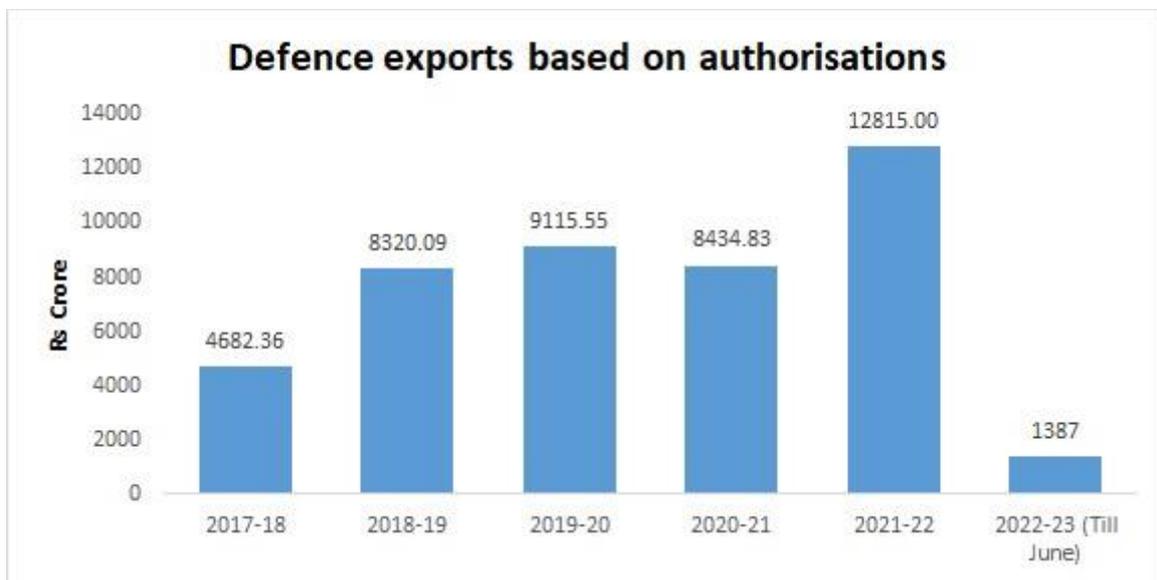
Industrial licenses issued to private companies for manufacturing of defence items

The Government is promoting privatisation in Defence Production. Defence Industry sector, which was hitherto reserved for the public sector, was opened up to 100% for Indian private sector participation in May, 2001. Since the opening up of Defence sector, a total of 584 Industrial Licenses

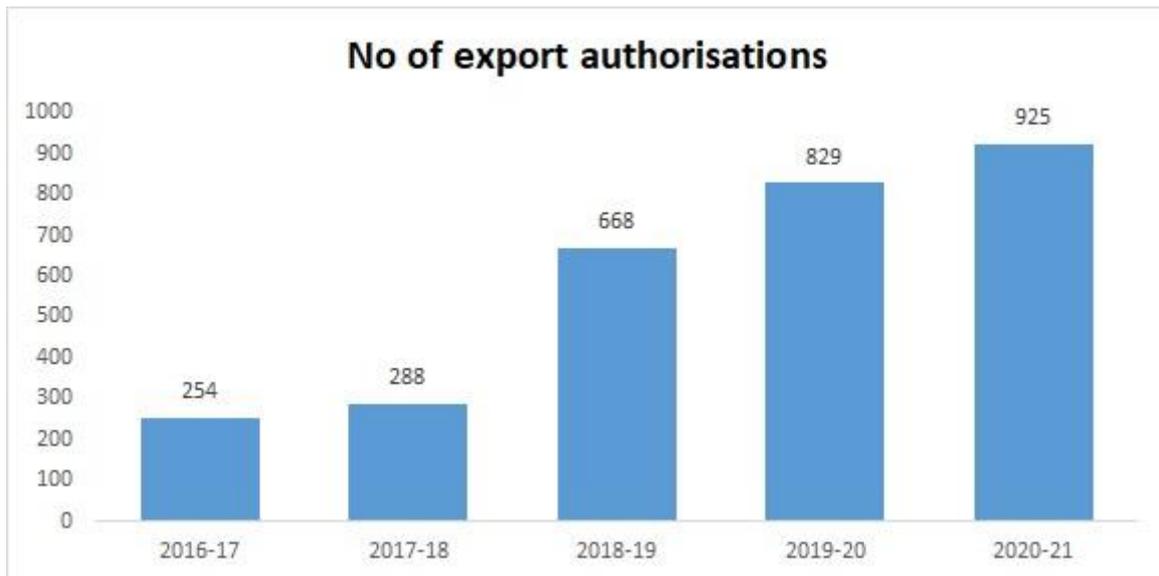
have been issued to 358 companies for manufacturing of various defence items. The initial validity of the Industrial License granted under the Industries (Development & Regulation) Act has also been increased from 03 years to 15 years. Increase in validity of Industrial Licenses has provided sufficient time and space for companies to start operations and manufacture without hindrance.

Defence exports

India exported around Rs 1,387 crore worth of defence-related exports based on authorisations during the first quarter of the financial year 2022-23 (April-June), on the back of multiple defence initiatives. The country's defence and technology related exports touched the highest-ever figure of Rs 12,815 crore in 2021-22, a 51.93% jump over Rs 8434.83 crore in 2020-21. The country's defence exports were worth Rs 9,115 crore in 2019-20, Rs 8320.09 crore in 2018-19, Rs 4682.36 crore in 2017-18 and Rs 1521.86 crore in 2016-17. The country's defence exports are mainly to countries like the US, the Philippines and other countries in South-East Asia, the Middle East and Africa.

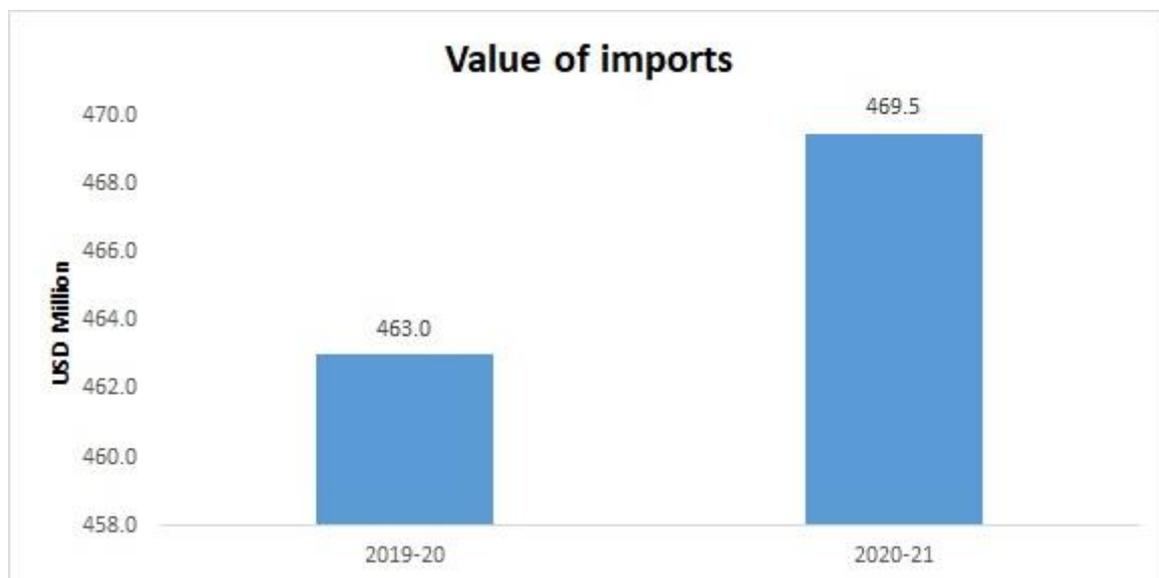


With the government's export-friendly policies to tap new markets, the defence ministry issued 925 export authorisations for different weapons and sub-systems in 2020-21, compared to 829 in 2019-20, 668 in 2018-19, 288 in 2017-18 and 254 in 2016-17. Department of Defence Production is the competent authority to issue 'Authorization' for the export of munitions list items i.e. Items mentioned in category 6 of SCOMET List notified by DGFT for the export of items specifically designed for military purposes. SCOMET item is an acronym for Special Chemicals, Organisms, Materials, Equipment, and Technologies and these are dual-use items that can be used for both civilian and military applications.

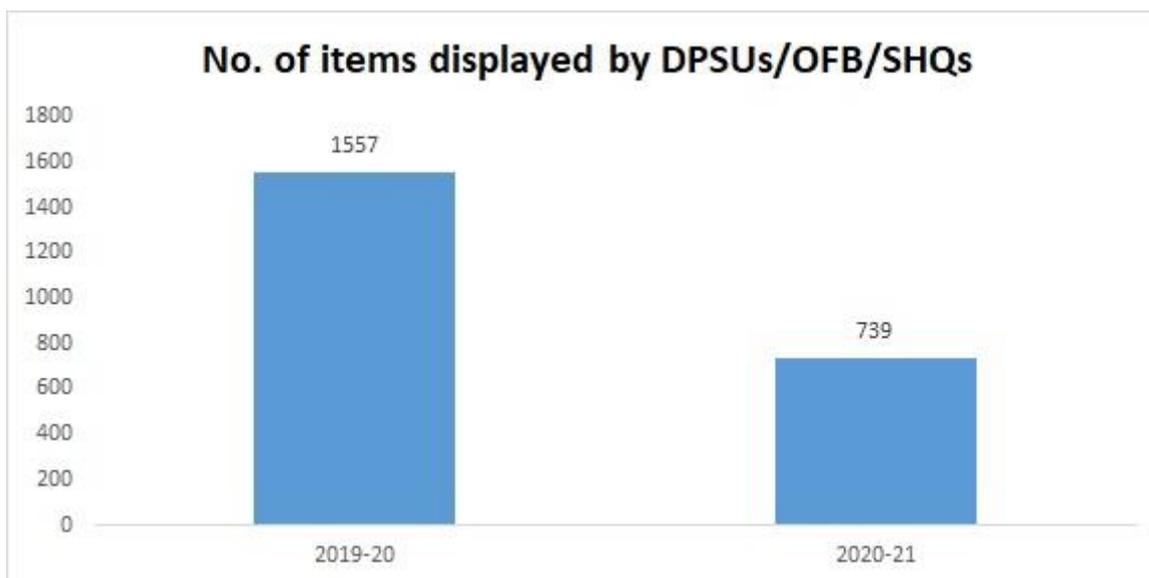


Defence imports

India's defence imports increased from \$463.0 million in 2019-20 to \$469.5 million in 2020-21. Though, to promote self-reliance and reduce imports, the Ministry of Defence has come out with a list of 2,851 items to put in an import embargo list in order to save Rs 3,000 crore annually. The government looks to reduce its reliance on imported military platforms and support domestic defence manufacturing, the Defence Ministry has set a timetable for a staggered import ban from December 2023 to December 2028. The government has approved a new list of 780 components and subsystems procured only from domestic industry.

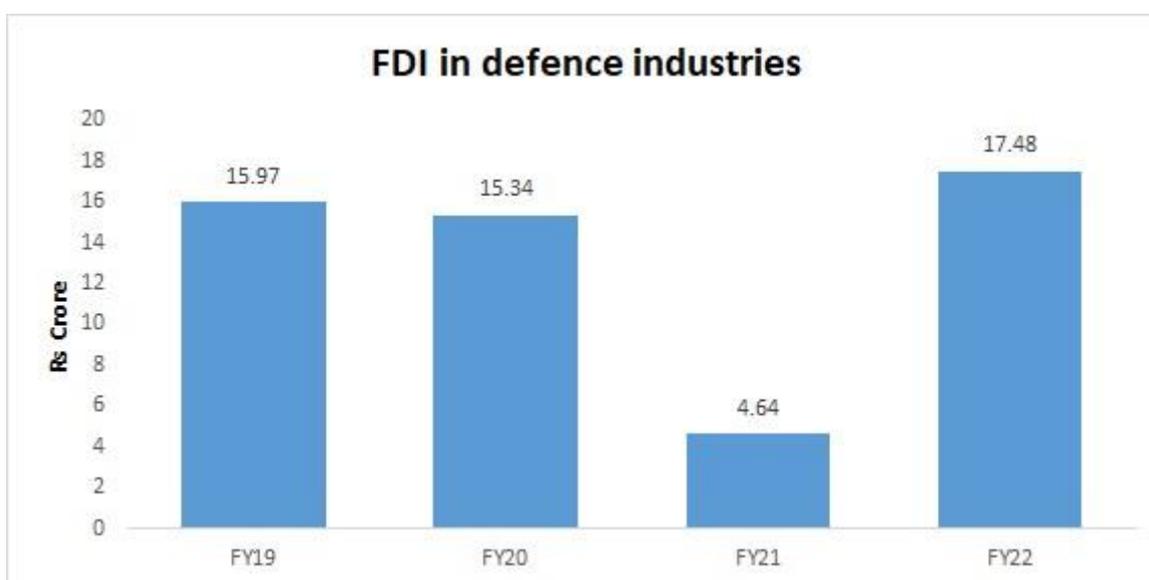


The number of items displayed by Defence Public Sector Units (DPSUs) /Ordnance Factory Board (OFB) and Service Head Quarters (SHQs) declined from 1557 in 2019-20 to 739 in 2020-21.



FDI in defence industries

The Government has liberalised and allowed Foreign Direct Investment (FDI) under automatic route up to 74% and up to 100% through Government route. FDI limit for defence sector has also been made applicable to Manufacturing of Small Arms and Ammunitions covered under Arms Act 1959. Further, foreign investment in defence sector is subject to other conditions of extant FDI Policy as amended from time to time. India has received around Rs 494 crore of foreign direct investment in the defence sector since revising the policy relating to it in September 2020. In FY22, the country received FDI of Rs 17.48 crore up from Rs 4.64 crore received in FY21. Meanwhile, the country had received FDI worth Rs 15.34 crore in FY20.



Recent developments

India bans import of 780 items in self-reliance push

The Defence Ministry has approved a fresh list of 780 components and sub-systems that will only be procured from the domestic industry. The defence ministry has set timelines for a staggered import

ban from December 2023 to December 2028 as the government wants to reduce dependence on imported military platforms and support domestic defence manufacturing. This is the third such 'positive indigenisation' list comprising line replacement units, sub-systems and components used for various military platforms, equipment and weapons to minimise imports by the defence public sector undertakings (DPSUs). The other two similar lists were published in December 2021 and March 2022.

Indian army signs a MoU with drone federation of India

The Army Design Bureau on behalf of the Indian Army has signed a MoU with the Drone Federation of India to collaboratively work towards promoting research, development, testing and manufacturing of drones, counter-drone and associated technologies that can assist the Indian Army in its operations. This MoU also signifies the unwavering commitment of the Indian Army in supporting our industry and the complete eco system to develop indigenous equipment and weapon systems in line with Atmanirbharta in defence manufacturing. The Army Design Bureau is the nodal agency of the Indian Army to be the facilitator for the R&D efforts with the Industry, Academia, DRDO and DPSUs to enable them to understand and appreciate user requirements in depth. This MoU between the Indian Army and the Drone Federation of India will promote efforts to handhold the industry and academia in order to assist them to develop niche technology and products for procurement by Indian Army.

Funding under TDF scheme of DRDO enhanced to Rs 50 crore per project

The government has approved enhancement of funding under Technology Development Fund (TDF) scheme of Ministry of Defence to Rs 50 crore per project from Rs 10 crore. The TDF scheme, executed by Defence Research and Development Organisation (DRDO), supports indigenous development of components, products, systems and technologies by MSMEs and start-ups. The TDF Scheme aims to provide a major fillip to the defence manufacturing sector by encouraging the industry to innovate and develop defence technologies in order to place India on the self-reliance trajectory. The scheme facilitates up to 90% of the total project cost and allows industry to work in consortium with another industry/academia. With the enhanced funding, the industry and startups will be able to develop more complex technologies for existing and future weapon systems and platforms. Till June 2022, 56 projects have been sanctioned under TDF scheme.

Government initiatives

Govt establishes two Defence Industrial Corridors

The Government has established two Defence Industrial Corridors, one each in Uttar Pradesh and Tamil Nadu. It has been envisaged to attract total investments of Rs 20,000 Crore in the two Defence Industrial Corridors of Uttar Pradesh and Tamil Nadu by the year 2024-25. The respective State Governments have also published their Aerospace & Defence Policies to attract and facilitate private players as well as foreign companies including Original Equipment Manufacturers (OEMs) for investments in these two corridors.

Govt launches iDEX framework

Innovations for Defence Excellence (iDEX) framework was launched by the Government with the aim to foster innovation and technology development in Defence and Aerospace Sector by engaging Industries including MSMEs, start-ups, individual innovators, R&D institutes and academia and promote self-reliance. Under iDEX framework so far, seven editions of Defence India Start-up

Challenge (DISC) have been launched. Under the iDEX route, the Government focuses on innovation and design & development and supports the start-ups and innovators for successful prototype development. Large number of start-ups have participated in various rounds of Defence India Start-up Challenge. So far, 136 start-ups have been engaged and 102 contracts have been signed for prototype development. Moreover, the Ministry has accorded Acceptance of Necessity (AoN) for 14 iDEX products, paving the way for placement of orders on the iDEX winners.

Defence Procurement Procedure revised

Defence Procurement Procedure (DPP)-2016 was revised as Defence Acquisition Procedure (DAP) - 2020, which is driven by the tenets of Defence Reforms announced as part of 'Aatmanirbhar Bharat Abhiyan'. In order to promote indigenous design and development of defence equipment 'Buy {Indian-IDDM (Indigenously Designed, Developed and Manufactured)}' category has been accorded top most priority for procurement of capital equipment. The 'Make' Procedure of capital procurement has been simplified. There is a provision for funding up to 70% of development cost by the Government to Indian industry under Make-I category, whereas Make-II procedure provides assurance to the industry for procurement. In addition, there are specific preferences for MSMEs under the 'Make' procedure.

Outlook

The India's defence industry is in bright spot and the outlook of the industry is optimistic in coming time with higher demand due to national security concerns. A strong developed domestic defense manufacturing sector is becoming a strategic necessity in the context of increasing geopolitical risks and an unstable neighbourhood. India depends on Russia for nearly 60% of its defence equipment, and the war in Ukraine has added doubts about future supplies. With government's support for domestic manufacturing, the industry can do well in coming time. In order to give a push to domestic defence industry, government has taken several policy initiatives in the past few years and brought reforms to encourage indigenous design, development, and manufacture of defence equipment in the country. Under the Make in India initiative, the Indian government focuses on minimising import dependence, increasing domestic capacity and modernising armed forces. It plans to achieve these by scaling up domestic manufacturing capacity by promoting local Micro Small and Medium Enterprises (MSMEs) and bigger defence manufacturers and by inviting foreign manufacturers to start operations in India. Moreover, the government has announced various reforms on aerospace and defence manufacturing policy to provide a fillip to defence equipment manufacturers in India. The government's support for FDI in the industry is also likely to support the growth. Besides, the defence ministry has set a goal of a turnover of \$25 billion (Rs 1.75 lakh crore) in defence manufacturing in the next five years, including an export target of \$5 billion worth of military hardware.