

# Six ways in which the new Defence Procurement Policy will be a game changer for MSMEs

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Predictably, the Defence Procurement Policy 2016 (DPP) unveiled by Defence Minister **Manohar Parrikar** has generated much commentary and as is always the case when a new policy is announced by the government - some debate as well. The consensus is that the new DPP will go a long way in addressing the issues that have afflicted **defence** procurement and acquisition over the years and, most hearteningly, it is expected to finally give a much needed boost to indigenous defence manufacturing.

However, much of the commentary has glossed over what the new DPP is going to do for that perennial bridesmaid of indigenous manufacturing - the Micro, Small & Medium Enterprises (MSME).

This by itself is not unusual because in any sector, big companies tend to hog the limelight, but ignoring defence MSMEs is ironical because of two key reasons. Firstly, the Dhirendra Singh Committee (the source of many of the good things in the new DPP) has acknowledged that 80 per cent of components, aggregates and assemblies of complex weapons systems and aircraft are made by MSMEs. Secondly, there are nearly 6,000 MSMEs across the country employing over 1.1 million people that supply components and

sub-assemblies to the defence PSUs, ordnance factories, DRDO and private companies. Both factors reveal that the real backbone of Indian defence manufacturing has all along been the MSME (and will be for times to come).

So, without further ado, let's look at six ways in which the new DPP promises to be a boon for MSME's.

**1. Recognition of MSME's role in defence**

**manufacturing:** The new DPP clearly recognises the critical role that MSMEs play in our defence eco-system. This looks like a fairly obvious point to make, but not if you've been a long suffering MSME faced with onerous and at times difficult to fulfil terms and conditions to make defence products.

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**2. Promotion of design-backed indigenous**

**manufacturing:** The new top priority procurement category of 'Indigenous Design Development Manufacturing' (IDDM) will back domestic companies that have proven competencies in design and innovation, very much the forte of MSMEs.

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**3. Stress on innovation:**

The move to fund 90 per cent of the developmental cost in the "Make 1" category, with a guaranteed return of the remaining 10 per cent if a successful prototype does not receive orders will encourage local development and innovation and will alleviate to some degree the high cost of capital that defence manufacturers (including MSMEs) have to deal with.

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**4. Assurance sans interference:**

In the Make 2 category, industry will fund its own prototypes but government will refund the entire development cost if there are no orders within two years of successful prototype development. Since there will be no direct Ministry oversight, manufacturers can work unimpeded. This augurs well for the entire industry including the larger established SMEs that have their own R&D.

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**5. Reservation for SMEs:**

All defence products

that will have a development cost of less than Rs 3 crore have been reserved for MSMEs in the Make 3 Category, which is a sensible move that will benefit the micro & small firms in this category.

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**6. Streamlining:** The new DPP also seeks to streamline the entire arms acquisition process by cutting down on the long delays that have become the norm. For instance, the concerned armed force will have to submit a draft "Request for Proposal" (RFP) along with the "Acceptance of Necessity" (AoN) thereby excising the normally long gap between AoN and RFP in one fell swoop.

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### **The One Dampener-Increased Offset Threshold**

Can there ever be a new government policy without at least one googly? The new DPP seeks to increase the offset threshold from Rs 300 crore to Rs 2,000 crore for foreign vendors, ostensibly to reduce the final price of defence equipment. Since the offset policy required 30 per cent of the contract value to be ploughed back into the indigenous industry, this will not only reduce foreign investments into Indian firms but also reduce business opportunities for a large number of Indian firms, particularly MSMEs.

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