Association of Aerospace Industries (Singapore)

***Aero*Intelligence™ Unit – Country Forecast Series**

INDIA

Since the early 1990s, India has gradually opened up its markets through economic reforms by reducing government controls on foreign trade and investment. Privatisation of public sector enterprises (PSEs) and the opening up of certain sectors to private and foreign participants has proceeded slowly and has been subjected to extensive political debate. The aerospace and defense industry was privatised only in 2001.

Growth in foreign direct investment (FDI) coupled with strong export growth have added to the buoyancy of the Indian economy. However, the main areas of concern have been the slow implementation of the economic reform process, the rising fiscal deficit, and poor infrastructure investment.

The Indian aerospace and defense industry is unique due to the overwhelming involvement of the government in the demand and supply of defense and aerospace products. The industry is predominantly government-owned and the domestic needs have been fulfilled largely through imports from Russia, Israel, and the United States. Global competitive pressures have necessitated the import of critical components from these countries where the technologies are matured and cost-effective. Indigenisation initiatives of the Government of India (GOI) are increasingly aimed at reversing this trend of excessive import dependency. The recent privatisation initiatives by the GOI have transformed the role of Indian private firms from supplying raw materials and semi-finished parts and components to producing high-tech defense and aerospace equipment.

Industry Overview

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Globalisation has made information security a key competitive factor, which could be a hindrance for the growth of the Indian aerospace and defense industry as countries become more cautious about outsourcing production for fear of knowledge diffusion.

The Indian aerospace and defense industry is transforming itself into a more export-oriented industry, which has the capacity to provide outsourcing opportunities for established firms in the United States and Europe and enhance domestic capability through extensive research and development programmes.

The Indian aerospace and defense industry shipments are expected to grow substantially over the period 2006-2010 due to the increased outsourcing opportunities coupled with the export competitiveness drive initiated by the government. Imports are gradually expected to decline with export growth led by the aircraft and spacecraft parts and navigation instruments segments/sectors.

India is currently one of the top 12 military spenders in the world. The Government of India has ushered in phased liberalisation into the defense industry realising the synergy and linkage effects that an enhanced domestic production could bring to the industry. The policy to deregulate certain select areas of the industry is aimed at import substitution through higher domestic production for meeting the expected domestic defense requirements. Key areas of growth within the industry are expected to arise due to the up gradation of production capacity, technology transfer, and modernisation of defense infrastructure.

<u>Trade and Tarrifs</u>

India has free trade agreements (FTAs) with countries in the South Asian region under the South Asian Free Trade Agreement (SAFTA) while negotiations are on for FTAs with other countries such as Thailand, Japan, Singapore, and countries of the Association of Southeast Asian Nations (ASEAN). A preferential trade agreement with Mercosur was also signed.
While most of India’s imports are from the Asian region, nearly a third of the country’s exports are to Asian countries. Imports are led by capital goods, electronics, and chemicals, while auto parts and pharmaceuticals dominate exports. Despite widespread trade liberalisation, India remains a closed economy, with imports representing only 19.8 per cent of the GDP while exports accounted for 17 per cent of the GDP in the fiscal year 2004-2005. Nearly 20 per cent of the import bill was due to oil imports as nearly 75 per cent of oil requirements are imported.

Although the peak custom rate was reduced to 20 per cent from the earlier 30 per cent, India remains extremely restrictive when it comes to trade mainly in the form of non-tariff barriers. It is estimated that nearly 15 per cent of all anti-dumping cases globally during the period 1995-2005 were initiated by India.

<u>Market Evolution</u>

- The Indian Market has come a long way from being at the lowest end of production spectrum, catering to the maintenance, repairs and overhaul of imported weapons to a stage where it can design and develop its own state-of-the-art systems.

- Pre 1953 — The industry was fragmented with nine private airlines. These airlines were incurring huge losses and operating with war surplus aircraft.

- Nationalisation in 1953 — All private airlines were nationalised and merged to form the Air India and Indian Airlines with the passing of Air Corporation Act, 1953.

- Post 1994 — The amendment of the Air Corporation Act, 1953 came into effect from March 1st 1994. The amendment removed the monopoly of the public carriers and allowed private airlines to operate in the domestic market.

- Growth of Low-Cost Airlines in the 2000s—Air Deccan started its operations in the no-frill segment. This segment has witnessed entry of many new participants such as Go Air, Spicejet and Indigo.

- Flow of FDI — The FDI in the segment is permitted to the level of 49 per cent and 100 per cent for non-resident Indians.

- Consolidation in the Industry—The industry has witnessed some consolidation activities with the Jet-Sahara Deal and Air Deccan-Kingfisher deal.