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India Manufacturing Barometer

Winds of change

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Contacts

PwC Strategy&

Bimal Tanna
Leader, Industrial Products
Partner, PwC India
bimal.tanna@in.pwc.com

Nilesh Narwekar
Partner, Strategy&
nilesh.narwekar
@strategyand.in.pwc.com

Sangeeta Singh
Principal Author
singh.sangeeta
@in.pwc.com

FICCI

Nisha Goel
Senior Assistant Director,
Manufacturing
nisha.goel@ficci.com

Aseem Khanna
Research Associate,
Manufacturing
aseem.khanna@ficci.com

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Abdul Majeed
Abhishek Tapadia
Kirtika Saxena
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Foreword

The Indian manufacturing sector seems to be emerging from an almost stagnant state in the recent past and heading towards a path of growth. This is exemplified by the significant growth of the sector from April to November 2015. This turnaround has been acknowledged by various multilateral organisations, including the International Monetary Fund, which recently described the Indian economy as one of the few ‘bright spots’ in the global economy. However, there remains room for pushing the growth even further, as the recovery is slow and fragile.

Recent initiatives by the Government of India, such as the *Make in India* campaign, deserve a special mention. FICCI is totally aligned with the *Make in India* campaign, which has already started bearing results. While growth and investments in some of the core sectors remain a matter of concern, the economy is expected to do better in months to come. Similarly, *Start-up India* will supplement the government’s efforts to encourage manufacturing in India.

The survey conducted by FICCI and PwC Strategy&—namely India Manufacturing Barometer—has brought out key aspects related to the sector, including the expectations of manufacturers for the next 10 to 12 months. The study highlights reforms related to land, labour and the goods and services tax (GST) as crucial means to attain our objectives.

We have a long way to go, and I hope this report will help in addressing and prioritising the issues concerning manufacturing in the short as well as the long term.

A Didar Singh

Secretary General, FICCI

February 2016

Preface

It gives me immense pleasure to continue our association with FICCI through the third edition of the India Manufacturing Barometer.

In the last year, the government has started to recognise and address the challenges faced by the sector through various initiatives. One such initiative, *Make in India*, aims to provide global recognition to the Indian economy, facilitate investment and build best-in-class manufacturing infrastructure. It emphasises the need for production in India, either by Indian companies or MNCs.

As per PwC's 19th Annual Global CEO Survey, 75% of Indian CEOs believe there are more growth opportunities for their company today than three years ago. However, several barriers need to be overcome to realise sustained growth, some of which can be resolved only through government intervention. While the industry senses the right signals from the government and is optimistic about long-term prospects, its current mood can best be described as one of cautious optimism.

The report summarises the views and expectations of industry leaders and presents their recommendations for creating a vibrant manufacturing sector.

I offer my sincere thanks to the CXOs who participated in this survey for providing us their valuable time and insights.

I hope you find this report interesting and useful, and look forward to any suggestions you may have.

Bimal Tanna

Leader, Industrial Products
PwC India

February 2016

Economic climate

The outlook for the Indian economy and its core sectors was upbeat at the beginning of the current financial year, with the government embarking on large-scale policy reforms and promising to deliver strong economic growth. While this positive mood continues, the appearance of several roadblocks on the domestic front and a demand slowdown globally and in emerging markets have forced sectoral players to rethink their short- and long-term strategy.

The big picture

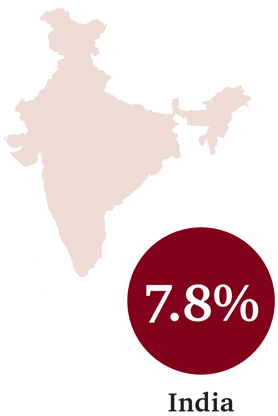
Despite the situation outlined above, figures for the next couple of years are encouraging. India has been declared a bright spot in the landscape of global economic development by both the World Bank and International Monetary Fund (IMF). The World Bank has projected growth in India at 7.8% in 2016–17 and at 7.9% in 2017–18, recognising the progress the country made with infrastructure improvement and the government's endeavours to boost investments, particularly in roads, railways and urban infrastructure. Meanwhile, IMF has kept its growth forecast for India unchanged at 7.5% in 2016–17.[1] IMF too attributed growth to recent policy reforms and a consequent pickup in investment, in spite of lower commodity prices.[2] In comparison, the World Bank's latest Global Economic Prospect report projected growth in China at a modest 6.7% in 2016.[3]

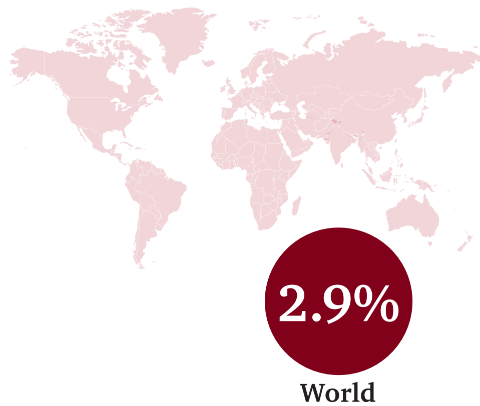
'At this point of time, it is wiser to be in India.'

– Narendra Modi, Prime Minister of India, at London's Guildhall in November 2015

In January 2016, leading economists at the World Economic Forum in Davos, expressed the view that the world economy is precariously balanced between continued recovery and a third leg of the global financial crisis.[4]

Exhibit 1
GDP growth projections for 2016





Source: Global Economic Prospect report, World Bank

Indian manufacturing sector: Opportunities for growth

The manufacturing sector in India will play a pivotal role in realising the projected growth. The Indian prime minister has stressed the fact that manufacturing, which has stagnated at around 16% of the GDP for several decades, requires a big push to reach 25% of the GDP by 2020.[5] The *Make in India* initiative was launched to transform India into a global manufacturing hub.

The opportunities highlighted by the prime minister in the manufacturing sector are listed below:[6]

- Setting up an India investment and infrastructure fund and tax-free infrastructure bonds for projects in rail, road and other sectors

- Opening up more sectors to foreign direct investment (FDI); building 50 million houses and setting up 100 smart cities

- Modernising the railway network and redeveloping stations and new railway corridors; generating 175 GW of renewable energy for transmission and distribution networks, bridges, national highways, and metro rail networks

According to government projections and media reports, India's manufacturing sector can touch 1 trillion USD by 2025. Further, there is potential for the sector to create up to 90 million domestic jobs by 2025.[7]

Until the end of August 2015, the central government received investment proposals of over 3.05 billion USD from various companies, a substantial chunk of which are linked to the *Make in India* initiative.[8] Given the roadblocks faced by certain key reforms, including those on land, labour and the goods and services tax (GST), it remains to be seen how many of these proposals will translate into capital inflow and investments.

Measuring the sector pulse

The Manufacturing Barometer indicates the current sentiment of business leaders from the manufacturing sector, the factors they perceive will impact their businesses over the next few months and the plans they expect to employ in order to address them. The survey covered 98 companies in eight key sectors: automobiles and auto components, cables and transformers, capital goods and heavy equipment, cement, chemicals, downstream metals, glass, and paper. Considering the significance of the *Make in India* initiative, in this edition, we expanded the scope of the survey to cover respondents' opinions on the campaign.

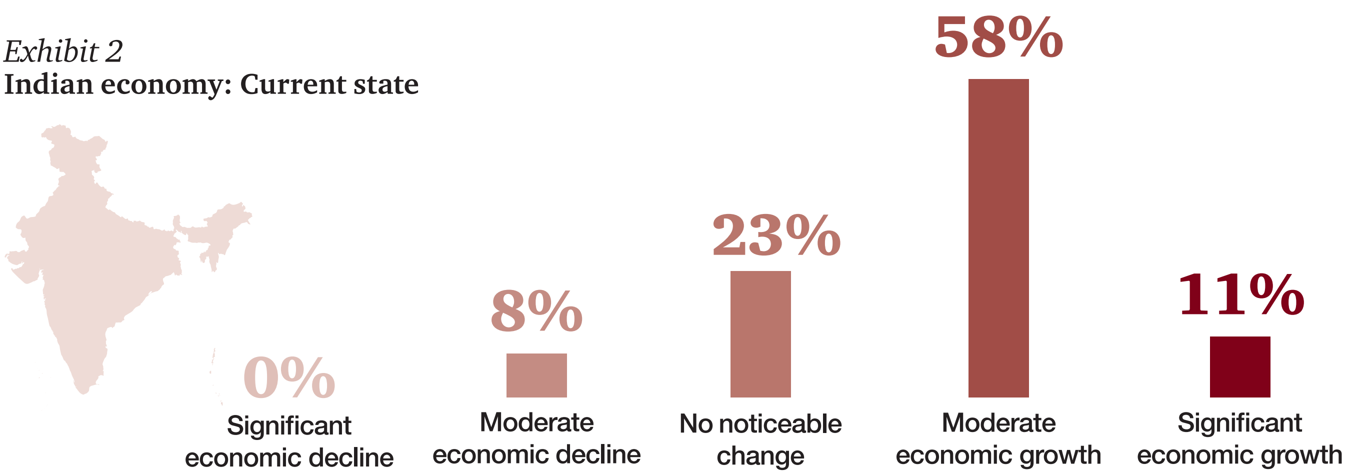
India versus the global economy

While the outlook for the global economy was not optimistic, the companies surveyed were relatively more positive about the Indian economy. Global growth slowed to 2.4% and is projected to remain below 3% in 2016, reflecting a slower pace than that envisioned. This trend is driven by a modest recovery in advanced economies and a more protracted slowdown across large emerging markets, including China.

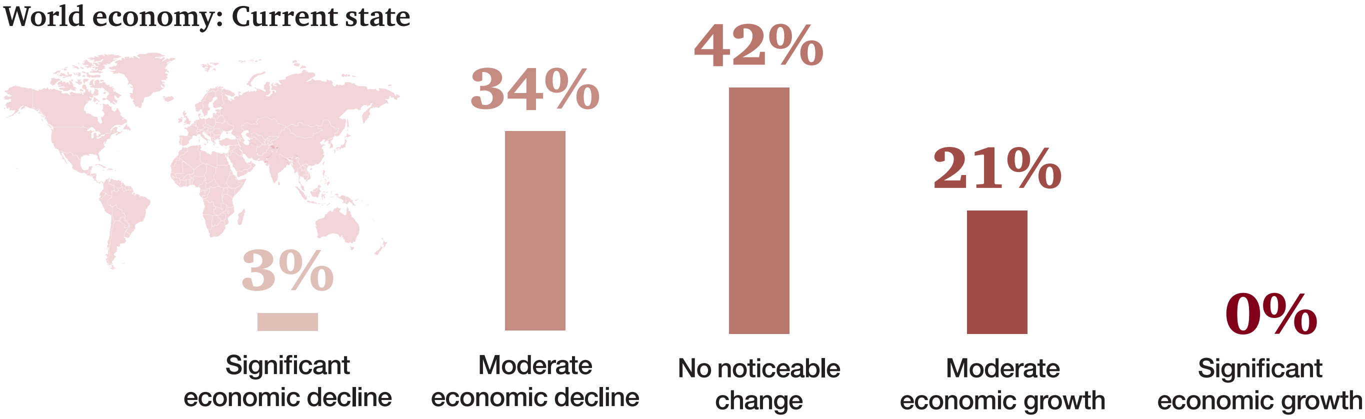
Moderate economic growth for the Indian economy

Of the surveyed respondents, 58% believed that the Indian economy would witness moderate economic growth, while 42% said they currently saw no noticeable change in the condition of the world economy. In fact, one-third of the respondents described the world economy as being in a state of moderate economic decline, as against only 1% in last year's Manufacturing Barometer survey.

Exhibit 2
Indian economy: Current state



World economy: Current state

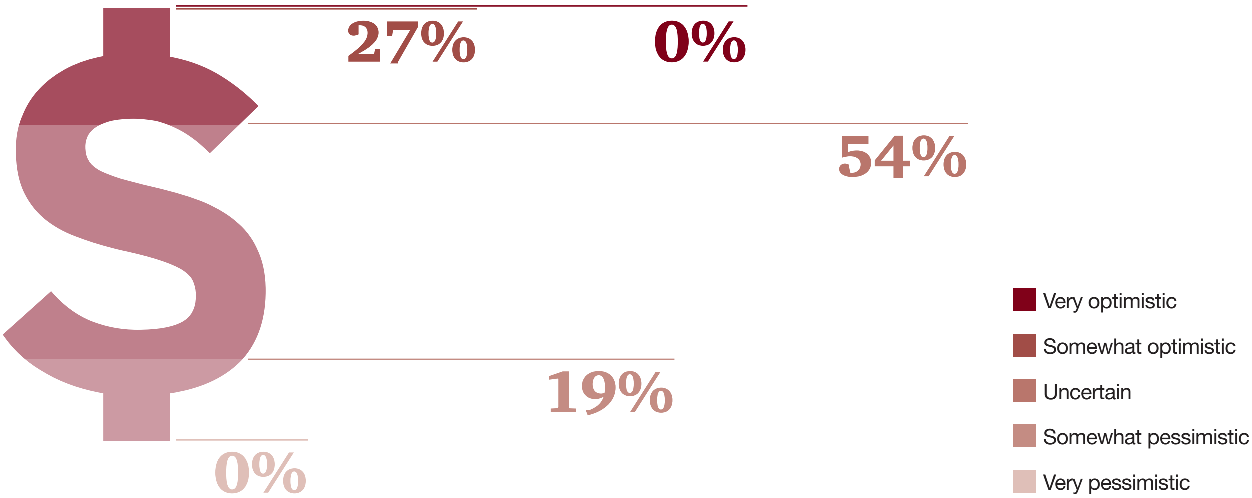


Source: Strategy& analysis

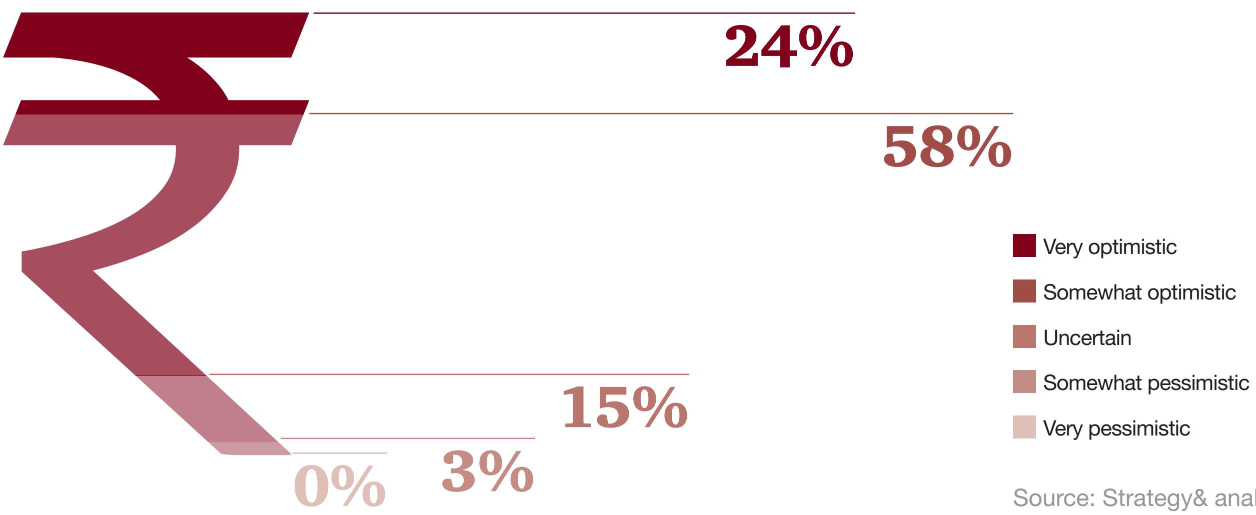
Optimism about the Indian economy

Only 58% of the respondents are somewhat optimistic of the prospects of the Indian economy for the coming year (refer to Exhibit 3), compared to 68% respondents in last year's survey. A majority of the respondents agreed that growth would be in the range of 7–8%. Views on the global economy were much more pessimistic as compared to that on the Indian economy, with 54% being uncertain. Given the 10% decline in optimism about the Indian economy as compared to the last report, respondents appear to be taking a cautious approach.

Exhibit 3
Prospects for the global economy in the next 12 months



Prospects for the Indian economy in the next 12 months

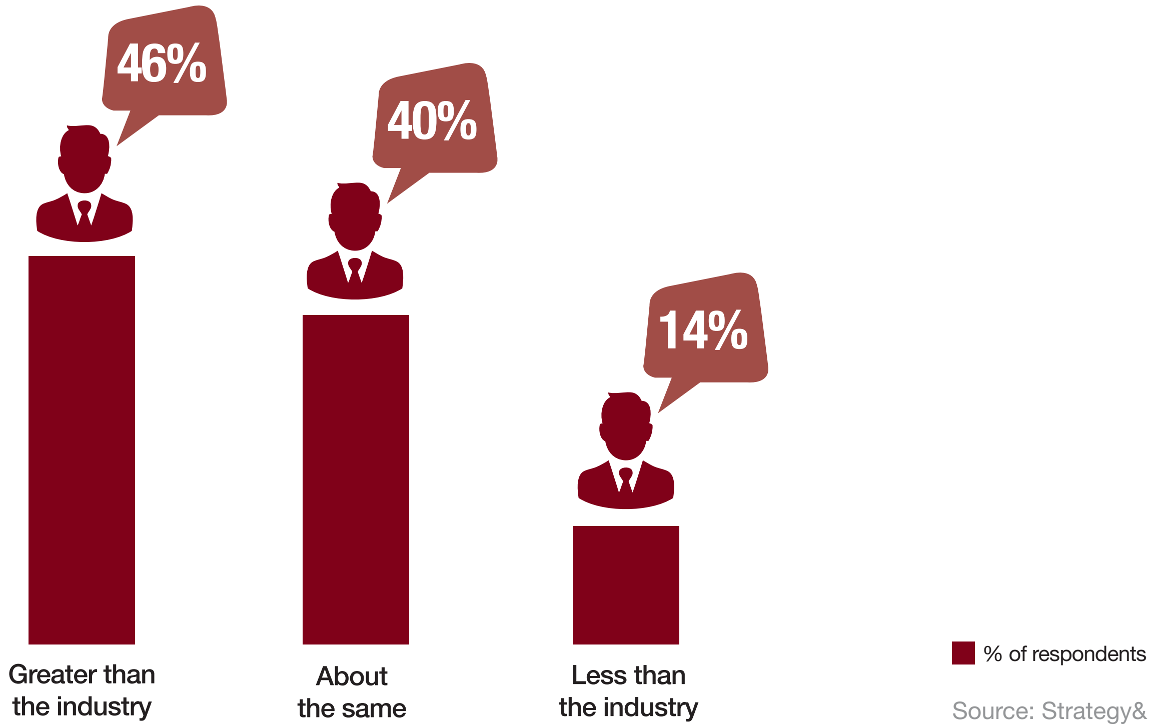


Source: Strategy& analysis

Industry revenue outlook for the next 6–12 months

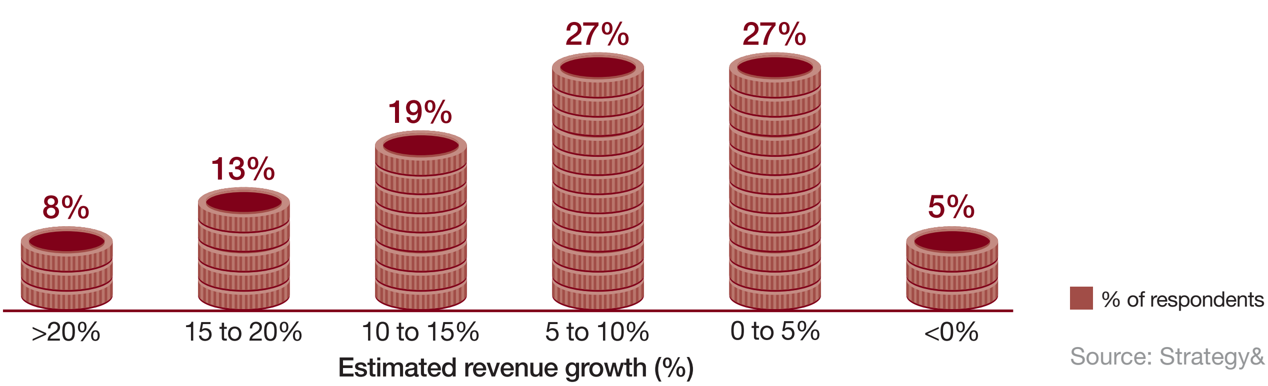
While 46% of the respondents said that growth of their own organisations outpaced that of the industry group they belonged to, 40% said their growth was on par with that of their industry. Only 40% respondents this year (as compared to 51% last year) believed that the estimated revenue growth next year of their own business would be at least 10%.

Exhibit 4
Estimated revenue growth (own business) versus industry growth



Source: Strategy& analysis

Exhibit 5
Estimated revenue growth (own business) over the next 12 months



Source: Strategy& analysis

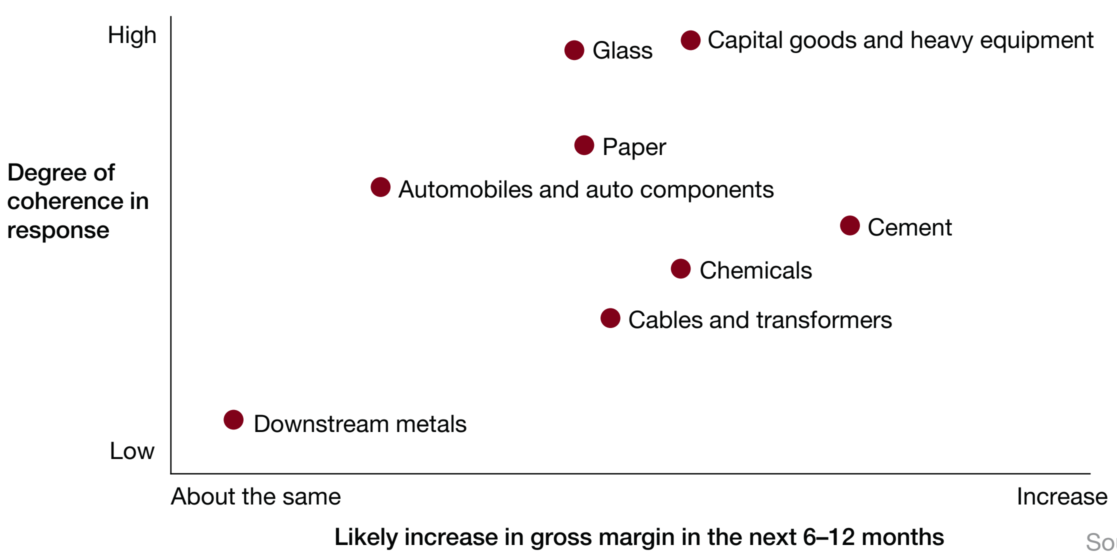
Sector-wise revenue outlook over the next 6–12 months

The respondents across sectors we surveyed were upbeat about the revenue outlook over the next 6–12 months. Their responses varied from 'moderately optimistic' to 'neutral'.

Exhibit 6
Sector-wise outlook for the next 6–12 months

Source: Strategy& analysis

Exhibit 7
Change in gross margins in the next 12 months



Source: Strategy& analysis

Change in gross margins across sectors over the next 6–12 months

The respondents were surveyed for their projections of the gross margins over the next 6–12 months—i.e. whether gross margins will 'increase', 'decrease' or 'remain about the same'. Overall, there was optimism that gross margins would increase.

However, there were differences between sectors. For downstream metals, the responses were distributed across 'increase', 'decrease', and 'remain about the same'. This resulted in an average expectation that gross margin would 'remain about the same' (X axis in Exhibit 7), with differences around the average resulting from the part of the sector value chain that the respondents operate in, and the interplay between input costs and prices expected for that part of the value chain.

The divergence in the responses across 'increase', 'decrease' and 'remain about the same' for respondents from the downstream metals sector resulted in the low coherence in responses (Y axis). In contrast, the respondents in sectors like glass, paper, and capital goods and heavy equipment were in agreement that the gross margin would increase in the next 6–12 months. This agreement resulted in these sectors having a high degree of coherence in the responses.

State of the industry: Key insights

An analysis of the responses received from the representatives of companies in each sector presented a mixed picture of the manufacturing sector as a whole. We now delve into industry-specific insights and nuances.

Automobiles and auto components

There is general optimism towards sector growth based on lower interest rates, product diversification, upgradation of vehicles, exports and lower commodity costs. This has encouraged many industry players, who are planning to add to the workforce and make capital investments with a focus on research and development (R&D).

Most companies feel margins have remained the same or improved in the last 6–12 months and expect them not to change or increase over the next 6–12 months. To better meet future challenges, several companies have launched initiatives like cost reduction. In addition to concerns regarding global trade, which are driven by the state of the global economy, overall concerns about demand and competition remain.

Cables and transformers

The outlook for this sector is mixed to optimistic, with a substantial number of the respondents of the view that the sector performed more or less in the same manner as the overall industry. Margin performance was mixed in the last 6–12 months. Although the view on new capital investments was mixed, most companies were in favour of capacity expansion. Further, there is optimism about the future, with a significant proportion planning to add to the workforce.

Factors that were perceived to help drive growth included growth of the distribution segment; revival of industrial demand for power; a stable currency regime and low interest rates; growth of housing, including in rural areas; infrastructure investment; government reforms; investment; project approvals and exports. Gross margins were expected to remain the same or increase in the next 6–12 months, primarily on account of commodity prices remaining low. The top concern was competition from imports.

Chemicals

The industry in India has seen single-digit growth due to depressed volumes from end-use markets and price pressures caused by a drop in commodity and oil prices. The industry growth rates and demand are not high enough to attract new investments and capacity expansions. Lacking the scale of the Chinese chemical industry and commoditisation, Indian companies are, at best, expected to grow at the same rate as the industry.

Going forward, 62% of the respondents expect margins to improve, with improved capacity utilisation resulting from a rise in demand in end-use industries such as agriculture, auto, detergents, buildings and construction.

Downstream metals

Largely dominated by steel, the industry is impacted by competition from imports, especially from China, who, it is claimed, are selling at or below cost. With depressed prices and cost pressures, margins are under stress for a majority of companies—57% of the respondents reported a drop in gross margins in the last 6–12 months. There are a few players, however, who are able to sell their output at a premium over other players, or who sell specialised products to specific end-use industries.

Companies, however, have a better outlook for the future, with the expectation that the government will extend support with a minimum import price, and that demand and price have in general bottomed out. The industry is focussed on recovery rather than renewed growth. The outlook for margins is largely linked to the outlook on price (including price support). Capacity additions coming on stream in the near term are outcomes of capex plans made earlier, as limited new investment plans are on the anvil.

Glass

The sector exhibited muted growth in the past year on account of sluggish growth in end-user industries (FMCG, liquor, auto and real estate) and an increase in the use of plastic and paper packaging. As a result, respondents are neutral about the revenue growth outlook for the next 12 months. Gross margins for most of the respondents have either remained the same or declined due to lower realisations and higher input costs.

Going forward, growth in real estate, auto and FMCG will drive revenues for the glass industry, as will the implementation of ministry guidelines on banning the use of plastic bottles in the pharmaceutical industry. Most respondents felt that gross margins would increase next year, mainly because of the internal measures of enhancing production efficiencies and strengthening sales capabilities.

Capital goods and heavy equipment

Most companies believe that demand will remain muted and competitive/pricing pressures will continue to dominate. Better housekeeping, however, will allow them to sustain or improve margins. Most companies plan to spend more on R&D, new product or service introductions, facilities/geographic expansion, and advertising and marketing. The outlook on capacity and workforce addition in the sector is not very optimistic.

Specific companies such as those in renewables expect to grow better than the industry in the next one year. Renewables also demonstrated higher growth than the industry average of 10% in six months. The overall price points for the capital goods and heavy equipment industry increased because of technology upgradations by end users and the resultant penetration of high-end technology. Further, while capacity utilisation remained moderate, product portfolio optimisation and appropriate pricing strategy have helped companies grow. Increase in prices did not result in steady margin growth due to internal operational inefficiencies.

Cement

Muted demand growth resulted in a decrease in margins and prices, low capacity utilisation (60–80%) and an average revenue growth of 7%, with regional disparities.

Going forward, however, players expect demand and margins to improve, driven by growth in the infrastructure sector due to policy and structural changes. The industry expects the government to support growth by giving a boost to the infrastructure and the housing sectors, introducing GST, and expediting the process of project approval. More than a third of the respondents plan to add more employees and expect additional capacity to come online in the next 6–12 months.

Consolidation is on the cards. Companies are planning business acquisition, spin-off or sale of certain operations/rationalisation of operations at old plants, and expansion/rationalisation of markets abroad. However, challenges remain. The top barriers to growth over the next 12 months include lack of demand and legislative or regulatory pressures (e.g. land acquisition laws, mineral leases).

Paper

Over the past year, the domestic paper industry has exhibited single-digit growth of around 6%, largely owing to low demand from end-user industries and increased imports. Gross margins for most of the respondents have either remained the same or declined due to lower realisations and higher input costs.

Going forward, growth is expected to be driven by the ‘writing and printing’ segment, but the ‘packaging’ segment is expected to give a boost to both revenue and margins. Players are moderately optimistic about the revenue outlook for the next year and select companies are planning to add capacity, especially in the packaging segment. Additionally, companies plan to focus on internal measures to enhance efficiency in manufacturing, which will lead to better gross margins.

Future growth

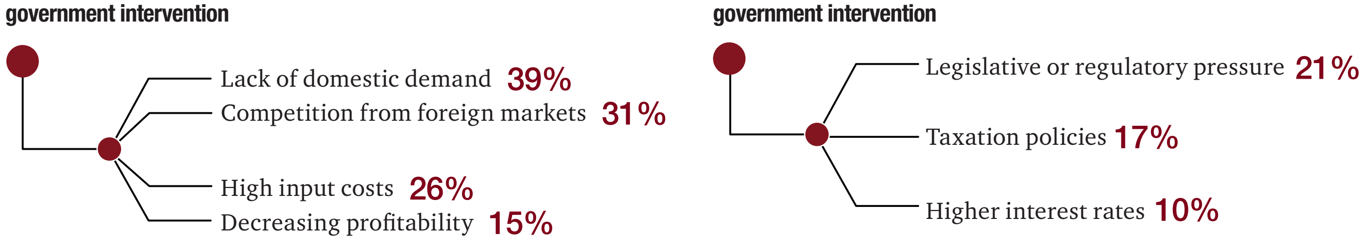
Policy paralysis, logjams in the implementation of key reforms, bureaucratic hurdles, besides supply chain bottlenecks and high input costs, have been affecting the Indian manufacturing sector for decades. Although some of these issues have been resolved, many remain to be addressed.

Respondents cited two categories of barriers to growth—those which can be resolved with government intervention, and those where other factors are also at play. Free-market forces—lack of domestic demand, competition from foreign markets and high input costs—have been cited as the top three under the latter category of barriers.

Exhibit 8
Barriers to growth

Barriers which cannot be resolved just by government intervention

Barriers which can be resolved by government intervention



Source: Strategy& analysis

To achieve growth, the survey indicates that respondents are looking to increase expenditure on R&D, new product/service introductions and facilities/geographic expansion. However, these responses should be interpreted with caution. In our experience, expenditure increased in areas like R&D are often projected but seldom materialise. Further, given the lack of domestic demand, competition from foreign markets and high input costs, in our view, it is unlikely that expenditure increases across heads will occur.

Exhibit 9
Heads for planned expenditure increase

63%
Research and development

51%
New product or service introductions

46%
Facilities expansion

45%
Geographic expansion

37%
Advertising and marketing

21%
Information technology

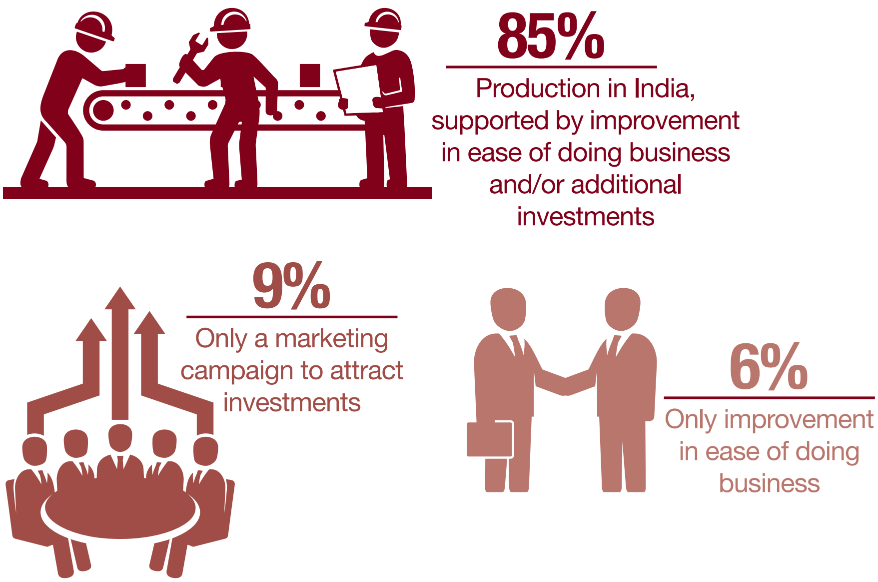
Source: Strategy& analysis

Making the most of the **Make in India** ***initiative***

At London's Guildhall, the prime minister highlighted the purpose of *Make in India*, namely to make India a better place to do business in. 'We are making it easier to invest in India. And believe me, we are making it even better to "Make in India".' He added that India has moved up by 12 ranks in one go according to the World Bank, and that the government was 'committed to take these corrections at the State, district and city level'.

Several campaigns have been launched by the current government. *Make in India*, *Swachh Bharat* and *Start-up India* are some of the recent ones. Of these, *Make in India* is most relevant to the manufacturing sector. Given the extensive press coverage of the political dimension of the *Make in India* campaign, this study attempted to understand its perception, impact and the required actions. Our conclusions are encouraging.

Exhibit 10
Industry perception of the *Make in India* initiative



Source: Strategy& analysis

- First, 85% of the respondents interpreted the campaign as encouraging production in India, either by Indian companies or by MNCs.

- Additionally, respondents within this group believed that the campaign has led to an improvement in ease of doing business as well as attracted greater foreign financial investment.

- Apart from the above 85%, another 6% of the respondents interpreted the campaign as exclusively promoting an improvement in ease of doing business.

- Only 9% of the respondents felt that the initiative was purely a marketing campaign to attract foreign financial investment.

- It is hence heartening to note that the campaign, through its simple language, is interpreted as a production-/manufacturing-oriented initiative.

The respondents indicated that the government has partially implemented the initiatives. Further, the responses differ across respondents based on their priorities. All of them share a common theme though—that the government is driving the campaign through key actions such as deregulation, labour reforms, and tax and duty exemptions. While these were cited most often, there are other

Exhibit 11
Recommendations to the government

1 Implement GST

2 Push infrastructure growth to boost demand for industries where infrastructure is an end market and to facilitate movement of goods

3 Improve ease of doing business (policies that are easier to understand, tax structures which are consistent in application, land and labour reforms)

Source: Strategy& analysis

measures as well: incentives for skill development, subsidies for R&D/technology, etc. However, there is additional ground to be covered by the government and the full impact of the initiative is yet to be felt by companies. While these recommendations have been acknowledged and necessary action has been promised, implementation has been slow.

Summary

While the outlook for the Indian economy remains positive, companies are demonstrating cautious optimism and indicating that their position on demand and investments could change depending on the global scenario. Expectedly, respondents were neutral to moderately optimistic about the industry outlook for the next 6–12 months. Further, there are signs that companies would rather wait and watch than go in for large-scale expansion. They are also expecting policy reforms in the form of implementation of GST, land and labour reforms, and large investments in the infrastructure sector, besides deregulation.

The fact that 85% of the respondents associate the *Make in India* campaign not only with a production emphasis but also with an improvement in ease of doing business, and/or perceive it as a marketing campaign to attract foreign financial investment suggests that the campaign will make an impact on their businesses.

Riding high on growth projections for the Indian economy, the manufacturing industry has the potential to grow in the coming year and thereafter. Resilience in the face of negative developments globally and the enabling environment created by the Indian government will provide further impetus.

‘Implementation remains a major challenge for the Indian economy and if it can deliver on its promises, the country will be the place to be… The gap in India has always been between the promise and the execution.’[9]
– Dr Raghuram G Rajan, Governor, Reserve Bank of India

Exhibit 12
Comparison of key indicators for business outlook

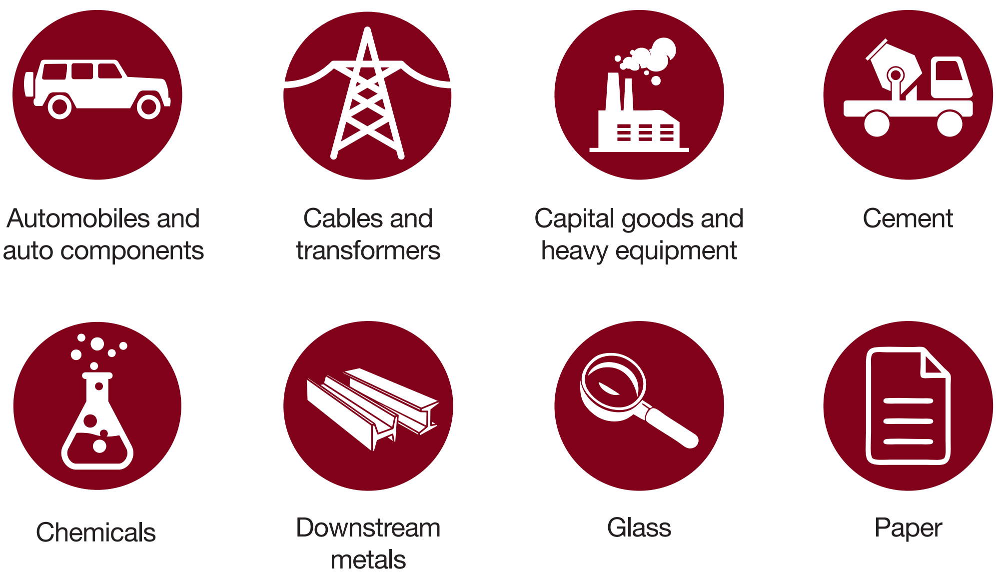
	2015	2014	2013
Condition of Indian economy today			
Significant economic growth	11%	6%	2%
Moderate economic growth	58%	75%	22%
No noticeable change	23%	19%	38%
Moderate economic decline	8%	0%	30%
Significant economic decline	0%	0%	0%
Prospects about Indian economy			
Very optimistic	24%	26%	0%
Somewhat optimistic	58%	68%	28%
Uncertain	15%	4%	54%
Somewhat pessimistic	3%	2%	14%
Very pessimistic	0%	0%	4%
Prospects for the Indian manufacturing sector			
Margins increased in the past 6 months	33%	37%	30%
Margins expected to increase in the next 12 months	36%	47%	54%
Key future business activities			
Expansion to new markets abroad	44%	61%	57%
Start at least one new strategic alliance or JV	19%	39%	43%
Planning to hire	41%	35%	35%
Planning major investments	44%	55%	40%

Source: Strategy& analysis, India Manufacturing Barometer (2013, 2014)

Survey demographics and research methodology

Interview period: 1 November 2015 to 10 January 2016

Exhibit 13
Industry sectors



Source: Strategy& analysis

Respondent profile: Chief executive officers, chief financial officers, chief operating officers and heads of strategy across the selected industries/companies

Methodology: The Indian Manufacturing Barometer is based on a survey conducted by PwC Strategy& and Avalon Global Research. The survey typically covers senior executives from a sample of Indian manufacturing companies.

About FICCI

Established in 1927, FICCI is one of the largest and oldest apex business organisations in India. FICCI's history is closely interwoven with India's struggle for independence, industrialisation and emergence as one of the most rapidly growing global economies. FICCI has contributed to this historical process by encouraging debate, articulating the private sector's views and influencing policy.

A not-for-profit organisation, FICCI is the voice of India's business and industry.

FICCI draws its membership from the corporate sector, both private and public, including MNCs. FICCI enjoys direct and indirect membership of over 2,50,000 companies from various regional chambers of commerce and through its 70 industry associations.

FICCI provides a platform for sector-specific consensus building and networking and is the first port of call for Indian industry and the international business community.

Our vision

To be the thought leader for industry, its voice for policy change and its guardian for effective implementation.

Our mission

To carry forward our initiatives in support of rapid, inclusive and sustainable growth that encompasses health, education, livelihood, governance and skill development.

To enhance the efficiency and global competitiveness of the Indian industry and to expand business opportunities both in domestic and foreign markets through a range of specialised services and global linkages.

Strategy& is a global team of practical strategists committed to helping you seize essential advantage.

We do that by working alongside you to solve your toughest problems and helping you capture your greatest opportunities.

These are complex and high-stakes undertakings — often game-changing transformations. We bring 100 years of strategy consulting experience and the unrivaled industry and functional capabilities of the PwC network to the task. Whether you're charting your corporate strategy, transforming a function or business unit, or building critical capabilities, we'll help you create the value you're looking for with speed, confidence, and impact.

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Endnotes

1. International Monetary Fund (https://www.imf.org)

2. International Monetary Fund (https://www.imf.org)

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