January 2019

India Manufacturing Barometer 2019

Building export competitiveness

Contents

Message from FICCI

Dilip Chenoy
Secretary General
FICCI

The Indian manufacturing sector has witnessed a steady recovery in the last 2 years, with the growth rate increasing from 2.8% in 2015–16 to 4.4% and 4.6% in 2016–17 and 2017–18 respectively.[1] Needless to say, a number of proactive Government initiatives like Make in India, a forward-looking and simple FDI Policy, and Skill India, along with the country's higher rank on the Ease of Doing Business Index, have been instrumental in reviving growth.

However, as we aspire to become a USD 5 trillion economy in the next few years, with manufacturing contributing USD 1 trillion, this journey needs to not only to continue but also be supported by deeper reforms and a more simplified regulatory regime in various areas. It will not suffice if manufacturing grows at a higher rate than GDP; the growth rate needs to be in double digits to ensure that adequate employment opportunities are available for our growing and young labour force.

Exports have an important role to play in this journey, for which we need to ensure that our exports are competitive on a sustainable basis. The global trade environment is becoming more and more challenging, with a number of high-technology areas and products playing a dominant role in trade. We need to support traditional sectors like textiles and leather, which are large employment generators, along with the emerging areas like electronics, defence, green technologies and digital technologies, which are going to dominate trade in future. This has been aptly noted by the latest World Trade Report of WTO,[2] which observed how digital technologies – and in particular the Internet of things, artificial intelligence, 3D printing and blockchain – affect trade costs, the nature of what is traded and the composition of trade.

Going forward, we are hopeful that the sector will grow at a higher rate and, more importantly, that exports can drive its growth. The India Manufacturing Barometer survey, conducted by FICCI and PwC, brings out the key aspects related to the sector, including manufacturers' outlook on the economy, the business environment for the next 12 months and factors that determine trade competitiveness.

I congratulate PwC India and the Manufacturing team at FICCI for bringing out the 5th edition of the India Manufacturing Barometer, and hope that you find this report useful.

Dilip Chenoy
Secretary General
FICCI

1 MOSPI
2 https://www.wto.org/english/res_e/publications_e/world_trade_report18_e.pdf

Foreword

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It gives us pleasure to continue our association with FICCI through the fifth edition of India Manufacturing Barometer.

Manufacturing as an economic segment accounts for a significant portion of the nation's wealth. It is anticipated that by 2025, India will have a USD 1 trillion manufacturing economy. The steps taken by the Government to ensure sustainable growth in the sector and a continuous inflow of foreign direct investments through several flagship initiatives and sectoral reforms seem to have started yielding dividends. Capacity expansion of key major global corporations that have done business in India successfully and entry of new manufacturing firms are contributing to exports and strengthening the industrial ecosystem. New investments in sectors such as telecom, food processing and automobiles have contributed to industrial growth.

In this edition of Manufacturing Barometer, we have sought the views of India Inc.'s C-Suite on the Indian economy and the business environment. The respondents have shared their perspectives on India's growth potential over the next 12 months, the impact of key reforms such as GST, changing nature of trade, and interventions needed from the Government to continue the growth trajectory. They have also highlighted the critical enablers needed for promoting export competitiveness.

Most respondents were upbeat about the industry and the future of the Indian economy, and acknowledged India's increasing importance to global markets. In the sectors shortlisted for this survey – namely automobiles and auto components, chemicals, electrical machinery, food processing, leather, pharmaceuticals and textiles – business leaders are expecting faster growth going forward compared to the current performance. They contend one of the key reasons for faster growth is the focus on Ease of Doing Business and introduction of reforms such as GST that are opening up new vistas for investments across the country.

In the past, the manufacturing sector relied on the domestic market as the primary source of revenue. But our survey brings to light the growing importance of exports to manufacturing companies in the future, with a focus on a good mix of parts – component trade along with end product trade, and the imperative to strategise for both types. Further, India Inc. seems to have begun placing greater emphasis on technology integration, including a renewed focus on R&D and innovation. To cement India's status as a global export destination, India Inc. expects the Government to focus on business ecosystem reforms and the industry's integration with global value chains.

We'd like to sincerely thank the participating business leaders across various segments of the manufacturing industry for taking time out to share their perspectives. We hope you find this report both insightful and relevant, and welcome any suggestions you may have.

1 Indian economy and business environment

In this section, we present the respondents' views on:

- Growth prospects of the Indian economy in the coming 12 months
- Growth of surveyed sectors in the coming 12 months
- Impact of the Goods and Services Tax on business

India: The global growth engine

India's economy is picking up and growth prospects look bright—partly thanks to the implementation of recent policies, such as the nationwide goods and services tax. As one of the world's fastest-growing economies—accounting for about 15 percent of global growth—India's economy has helped to lift millions out of poverty.[1]

- International Monetary Fund (IMF)

The IMF's positive sentiment towards the Indian economy is echoed by other major agencies such as the World Bank and United Nations Development Programme (UNDP), and is a testament to their confidence in the country and the expectation that it will drive global economic growth.

In 2017, India overtook France to become the sixth largest economy in the world, and it is expected to displace the UK and climb to the fifth position in FY 2018–19. This is impressive considering the overall strain the global economy continues to experience.

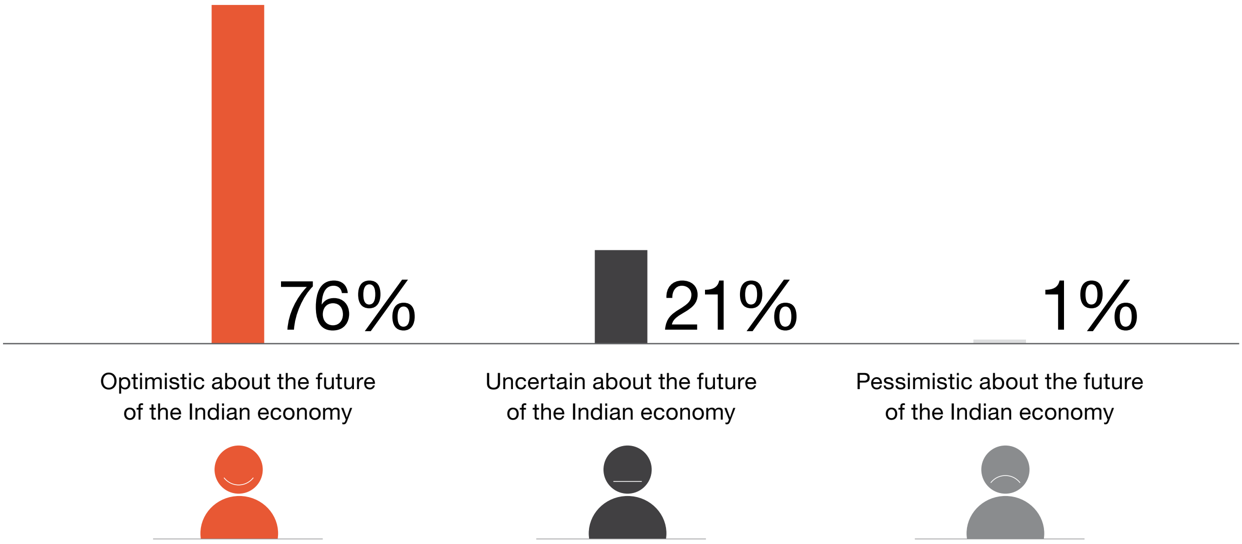
Increasing investor confidence has been one of the focus areas of the Government. Initiatives such as Make in India and associated reforms on foreign direct investment (FDI) and Ease of Doing Business (EoDB), Startup India, and Digital India have played a major role in achieving this goal.

India has demonstrated the ability to continue on its robust growth trajectory. By integrating investor-friendly policies with a strong focus on digital governance, the country has firmly placed itself on the path of creating a self-sustaining ecosystem, which will encourage diversification of business segments and create avenues for the development of manufacturing.

1. https://www.imf.org/en/News/Articles/2018/08/07/NA080818-India-Strong-Economy-Continues-to-Lead-Global-Growth
2. https://www.imf.org/en/Publications/CR/Issues/2018/08/06/India-2018-Article-IV-Consultation-Press-Release-Staff-Report-and-Statement-by-the-Executive-46155

India Inc. remains positive about the economy's growth prospects, in sync with the projections of international development agencies

View on the future of the Indian economy (coming 12 months)



*2% did not respond to this question

A majority of the respondents were upbeat and confident about India's positive growth performance. Most also believed that India has the potential to grow at an average rate of 7% or more in the next 12 months. This is aligned with the projections of international development agencies such as the World Bank Group and IMF, as shown in the table below.

Economy growth projections

Country/region	Expected GDP growth rate (%)					
	2018	2019	2020	2021	2022	2023
India	7.3	7.4	7.7	7.7	7.7	7.8
China	6.6	6.2	6.2	6	5.8	5.6
United States	2.9	2.5	1.8	1.7	1.5	1.4
European Union	2.2	2	1.8	1.7	1.7	1.6

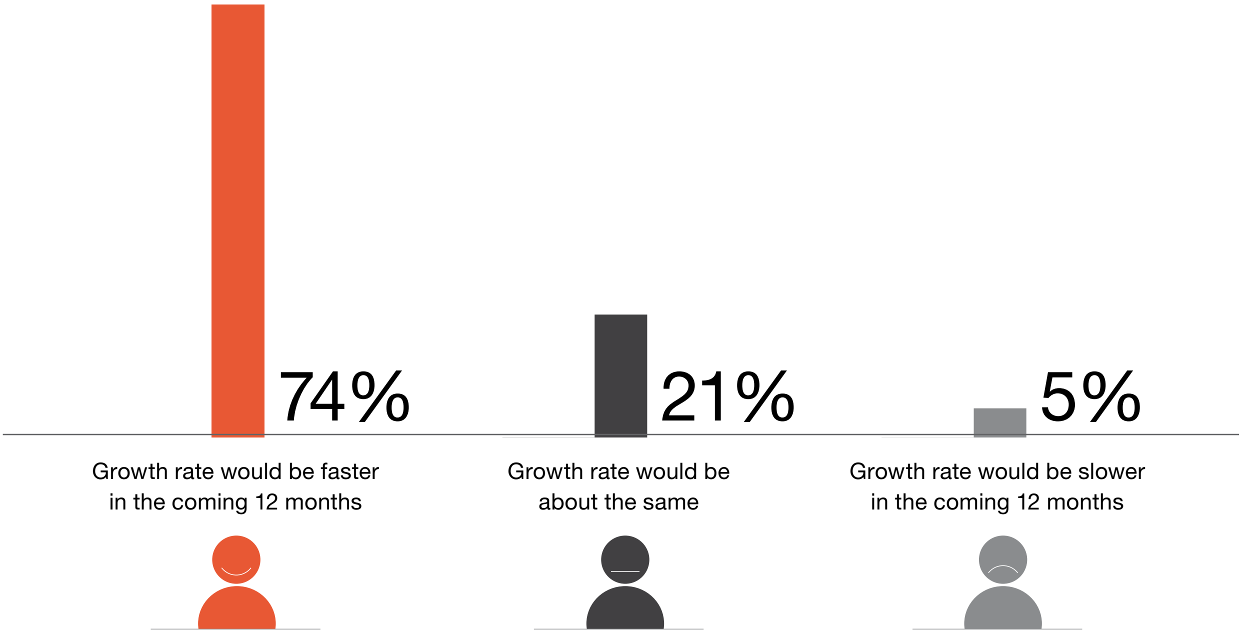
Source: IMF

Country/region	Expected GDP growth rate (%)		
	2018	2019	2020
India	7.7	7.8	7.9
China	6.6	6.4	6.3
United States	2.9	2.7	1.9
European Union	2.5	2.1	1.8

Source: World Bank

Business leaders anticipate faster growth in their sectors in the coming 12 months

View on the growth of their respective sector (coming 12 months)

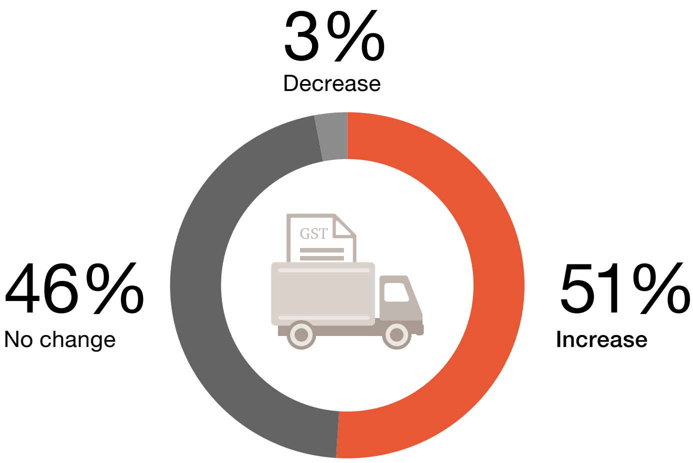


Surveyed companies believe that the expanding domestic market, complemented by emerging industry trends such as digitisation and automation, improvement in EoDB, increasing spend on R&D activities, and infrastructure development, is enhancing the growth prospects of their respective sectors.

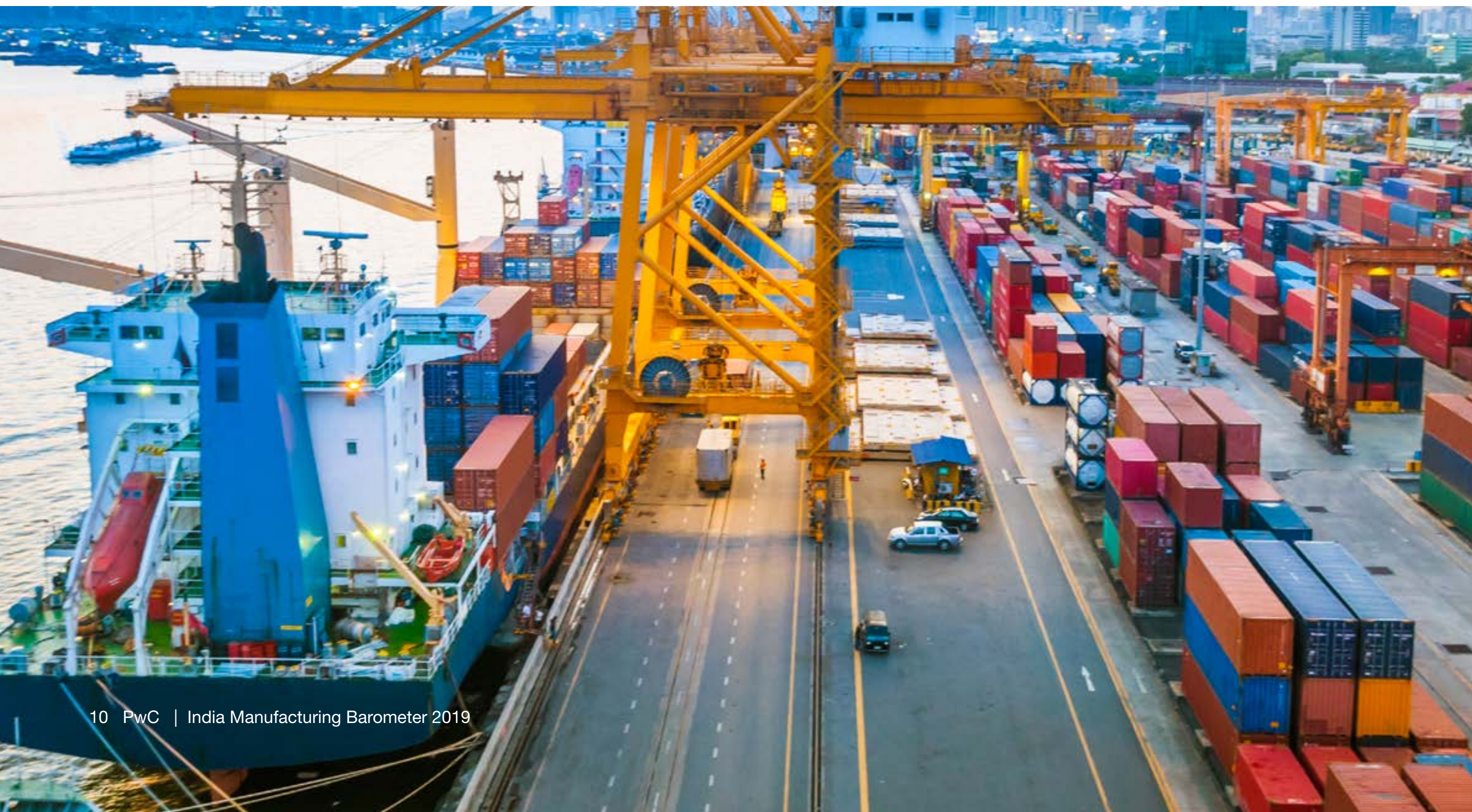
58% of respondents believe that their sector would grow faster by at least 5% in the coming 12 months.

India Inc. finds that speed and ease of logistics have improved on account of the Goods and Services Tax

GST's role in easing logistics and related processes



Introduced in 2017, GST was one of the most anticipated tax reforms in India, and has had far-reaching implications on how businesses will operate in the country. While GST provides a simplified, single tax regime in line with the tax framework applicable in several major economies across the globe, it had a huge impact on the supply-chain and associated mechanisms for the industry. The industry has responded by taking this as an opportunity to redefine supply-chain models, customise IT processes and rationalise tax costs.



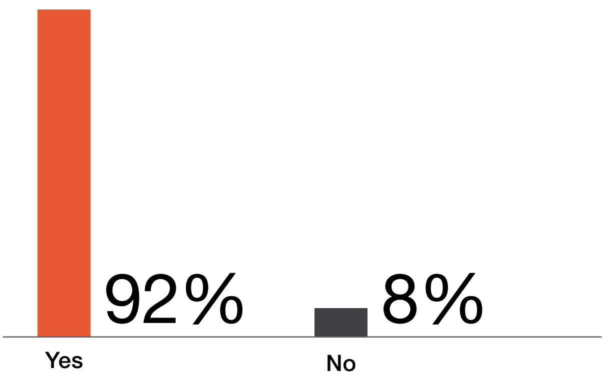
A majority view GST as the right policy measure to boost investments and foster economic development

India Inc. believes that the introduction of GST will provide new investment opportunities. While earlier investments were limited to certain locations based on a mix of fiscal and non-fiscal advantages, introduction of GST will help attract foreign and domestic investments across new locations.

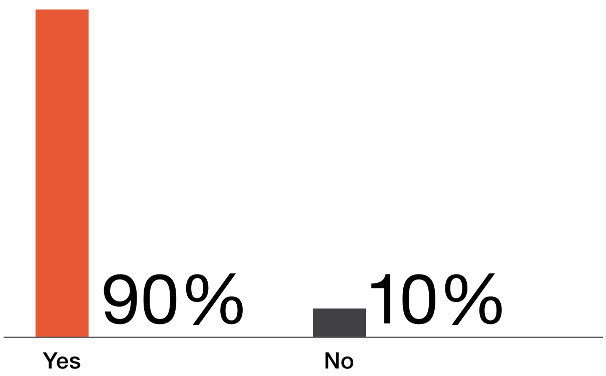
As the GST journey progresses, it has become clear that this is not merely a tax reform but a reform of the entire business scenario. Due to its multifaceted impact, GST has become a vital concern for every company's top management. This is evident from the unanimous belief among CEOs that the GST system would improve over time and lead to the overall growth of their industry in the long term.

Participants consider GST as an enabler for growth

Do you expect the GST system to improve further over time?



Do you believe the GST system will boost growth in your sector?



2 Export competitiveness

In this section, we present the respondents' views on:

- Current sources of demand
- Factors responsible for imports
- View on future import scenario
- Factors responsible for exports
- View on future export scenario
- Factors affecting export competitiveness

Export competitiveness

More than 60% of global trade consists of trade in intermediate goods and services. Further, GVC trade accounts for 30% of the GDP of developing countries.[3]

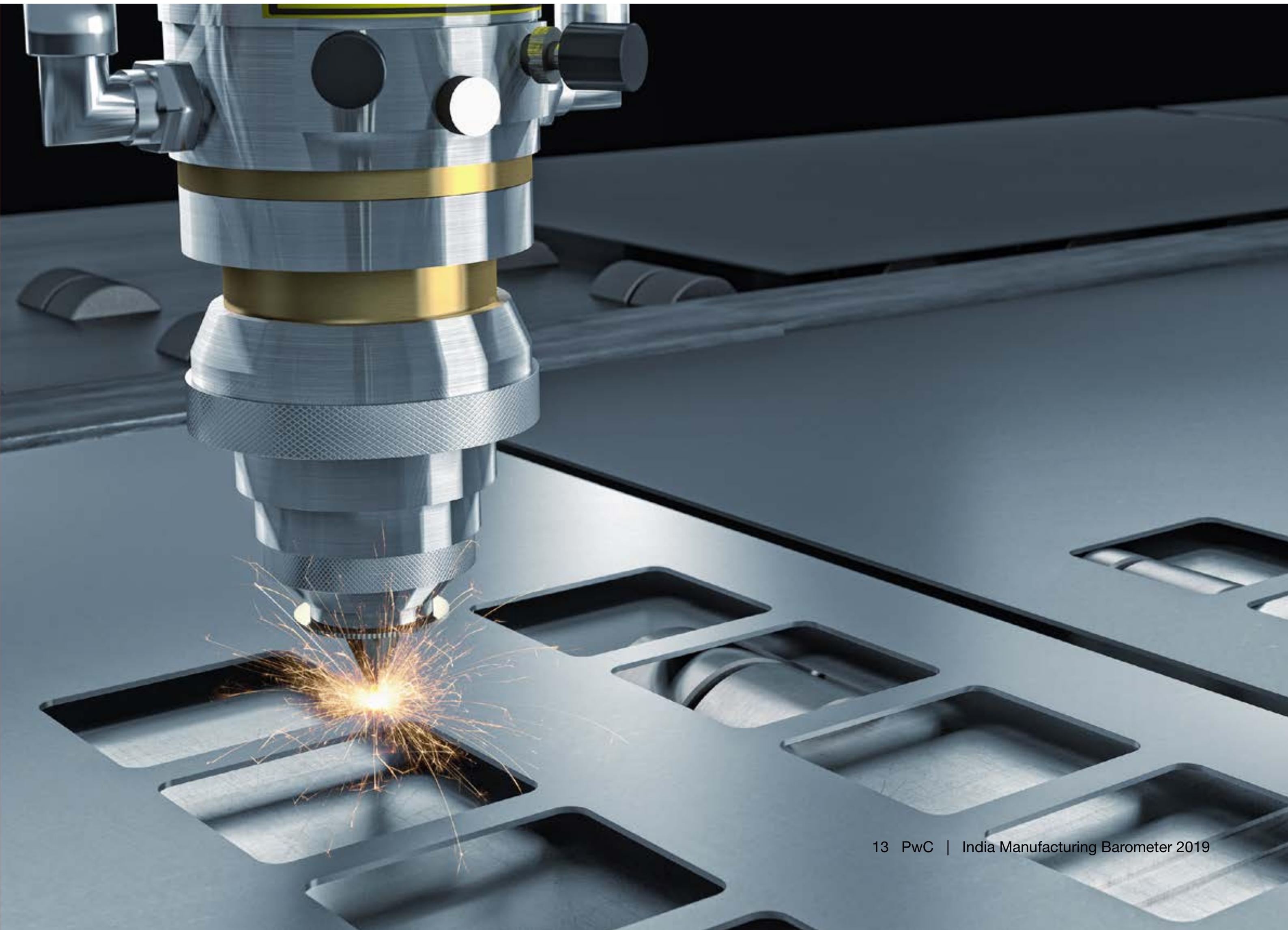
- United Nations Conference on Trade and Development

In the current global economic scenario of integrated value chains and connected production networks, trade is an important facilitator for an industry's development. Even with growing protectionism in global economies, companies have continued with their expansion plans, especially on diversifying and optimising their respective production networks, resulting in higher exports for their host economies.

Global value chains (GVCs) are becoming the new paradigm of domestic manufacturing and international trade. GVCs advocate fragmentation of production across the globe as per each economy's competitive advantage and selective specialisation. Since production takes place in a fragmented manner, it helps a country realise economies of scale and catalyse structural transformation by creating new linkages.

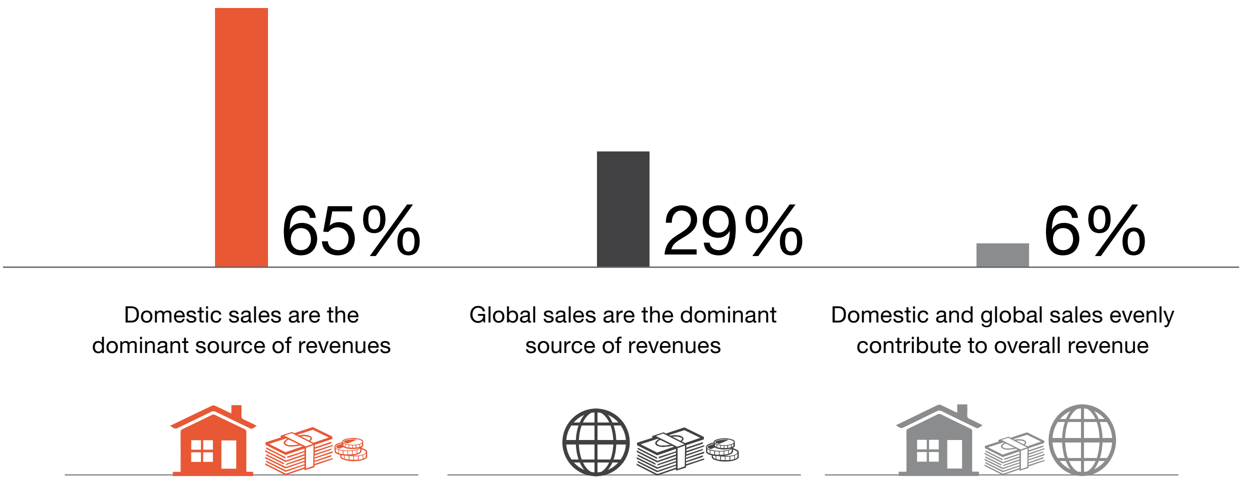
Government initiatives such as Make in India have been envisaged to make India a manufacturing hub for exports, generate large-scale employment and increase income levels. To some extent, this will also result in import substitution and help the country to cater to its own needs. Further efforts into R&D and product development are ongoing to make India integrate better into the connected economy.

3. https://unctad.org/en/PublicationChapters/wir2013ch4_en.pdf



Domestic market remains a major demand driver for India Inc.; business leaders expect an increase in global sales, going forward

Domestic versus global share of revenues

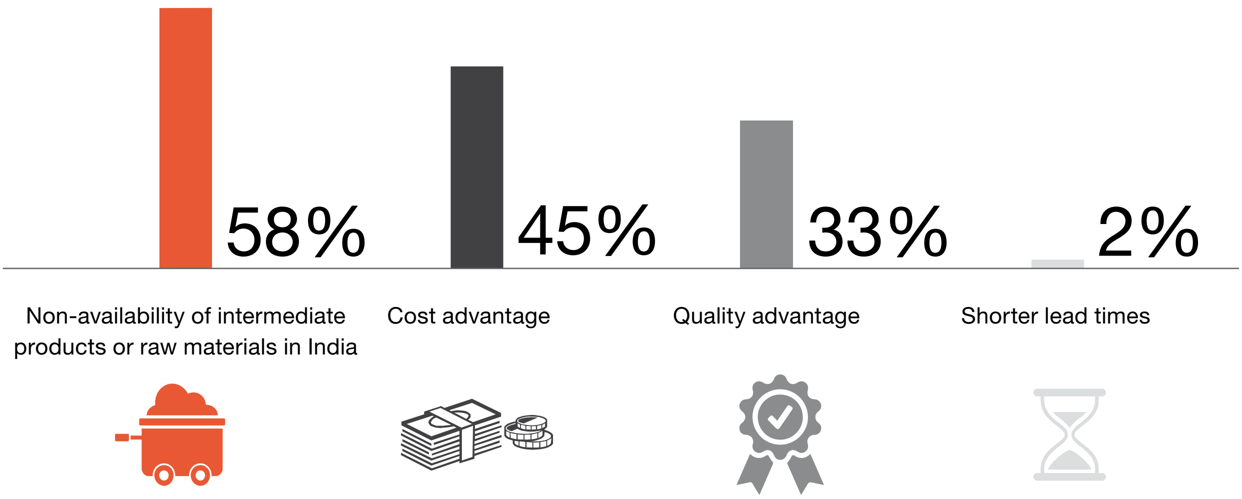


The survey indicates that India is seen as a major market by both domestic and multinational manufacturers. While domestic demand has been driving manufacturing in the country, going forward, business leaders expect global demand to play a larger role in stimulating the expansion of the manufacturing industry in India and spurring future sales of their companies.

85% of business leaders anticipate an increase in turnover from global demand in the future.

Imports are primarily on account of non-availability of intermediate products or raw materials in India

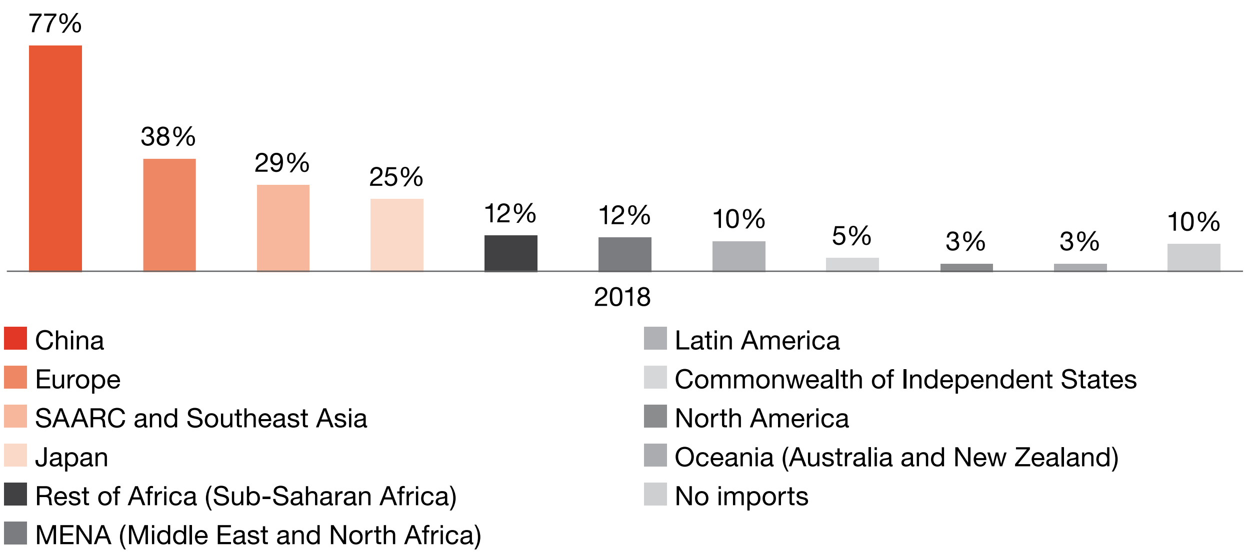
Primary reasons for import of raw material and intermediate components



Despite the fact that non-availability of intermediates/raw materials is stated as one of the primary reasons for import, industry captains underlined cost and quality advantage as two other significant reasons. They were of the opinion that corrective measures could significantly reduce the import basket.

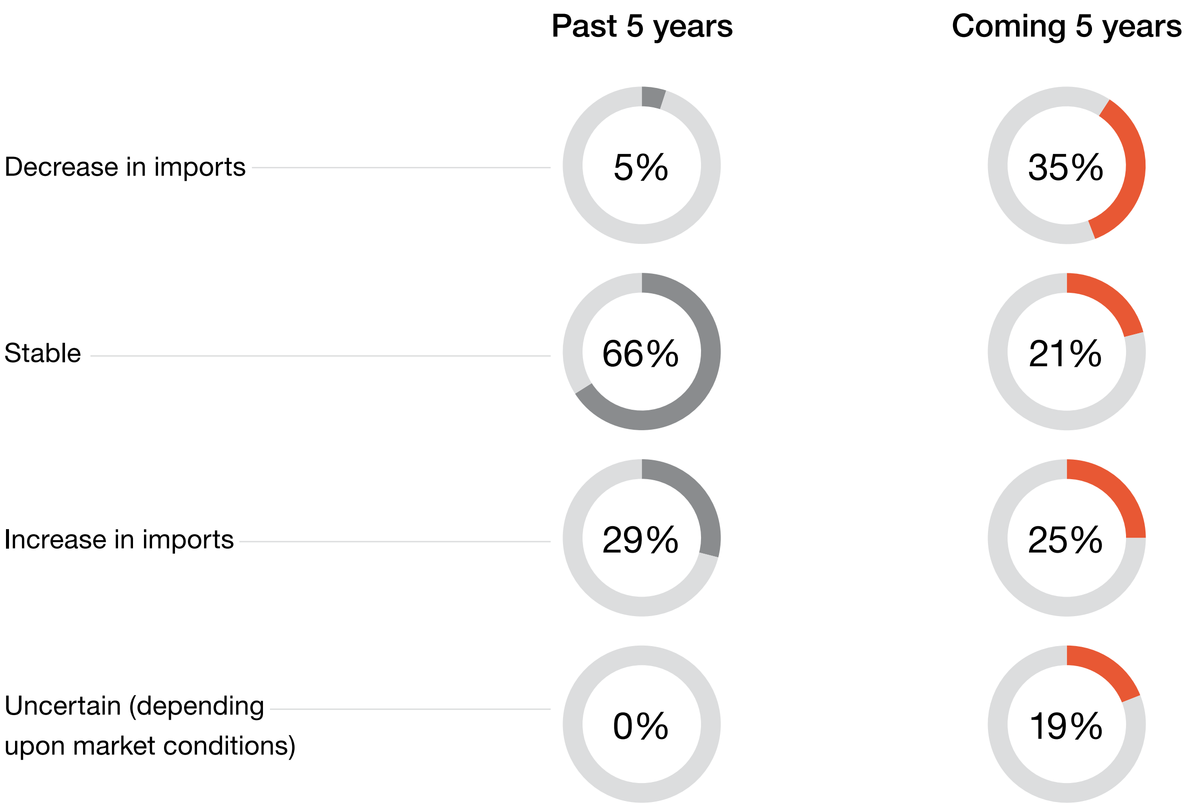
China continues to be a major supplier to India Inc.

Europe, Japan, SAARC and Southeast Asian countries are the other major suppliers of raw materials and components.



A majority expect a reduction in dependence on imports going forward

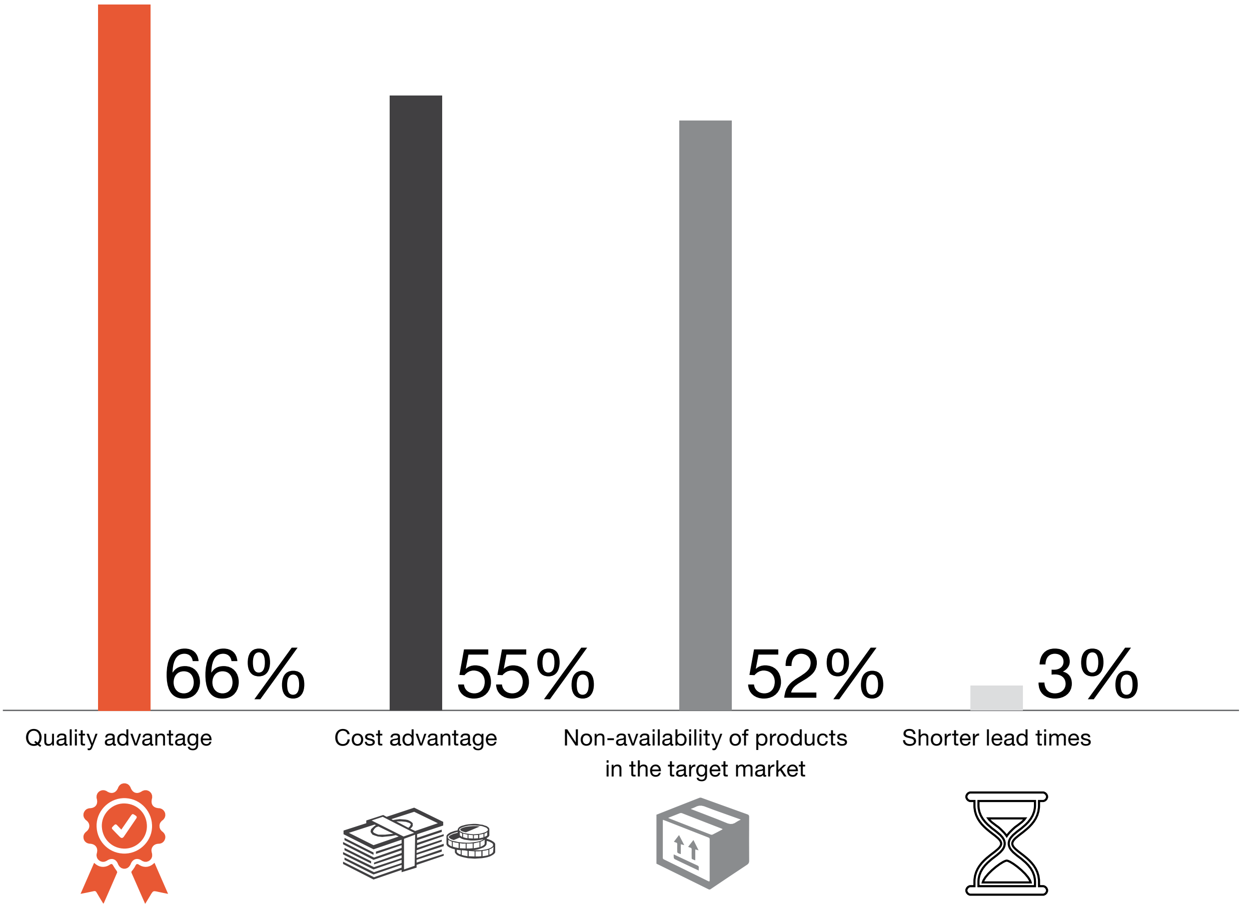
Dependence on imports of raw materials and intermediate components



While only 5% of the respondents witnessed a decrease in import share of their raw material and components over the past 5 years, an impressive 35% were optimistic about decreasing import share in the near future. An increase in domestic sourcing is seen as a positive sign for domestic manufacturing, which would eventually translate to economic growth and employment generation. However, a quarter of respondents predicted an increase in import dependence in the future.

India Inc. believes that quality advantage is now one of the key enablers driving their exports

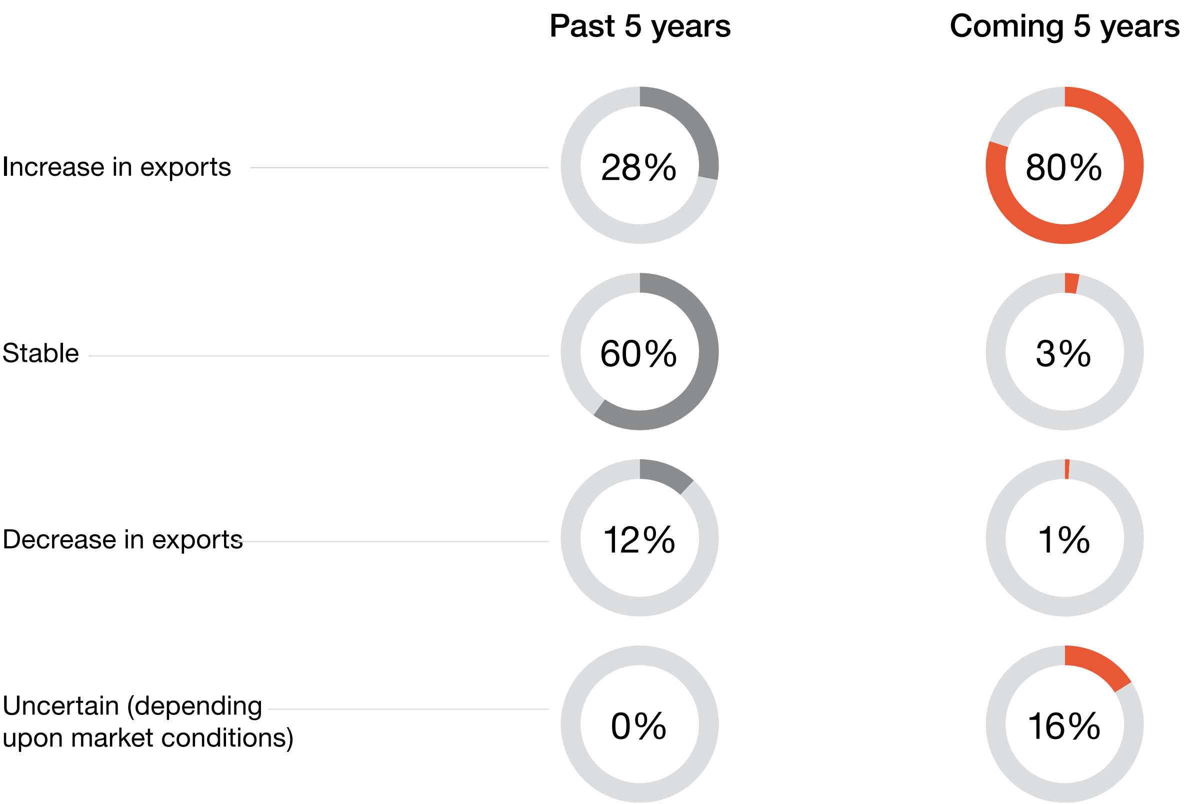
Key export drivers



While cost advantage remains one of the major contributing factors to export competitiveness, India Inc. believes that quality advantage has become the key differentiator for products from India vis-à-vis other exporting nations.

India Inc. is confident of increasing exports in the next 5 years

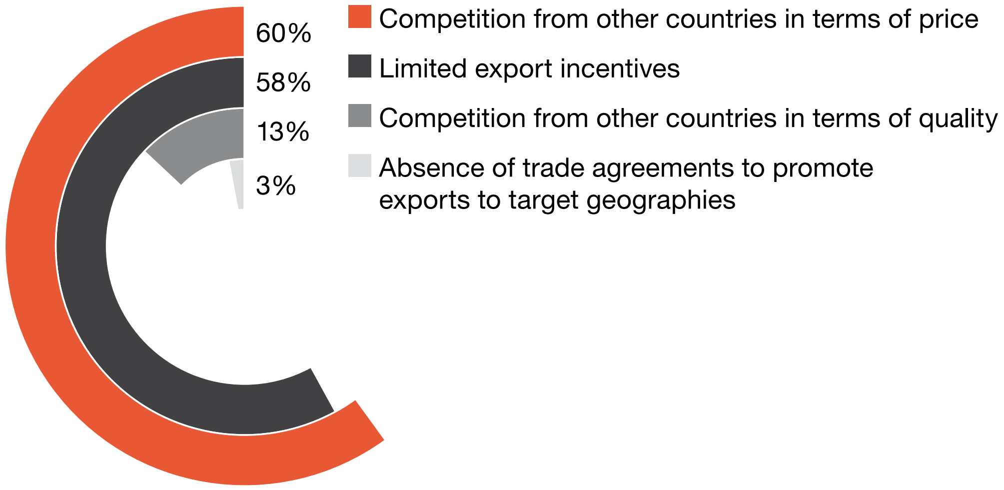
Indian export scenario and outlook



While 28% of the respondents witnessed an increase in the share of their revenue from exports over the past 5 years, a whopping 80% were optimistic about increasing their export share in the near future.

Cost competitiveness and export incentives are areas where India Inc. expects intervention

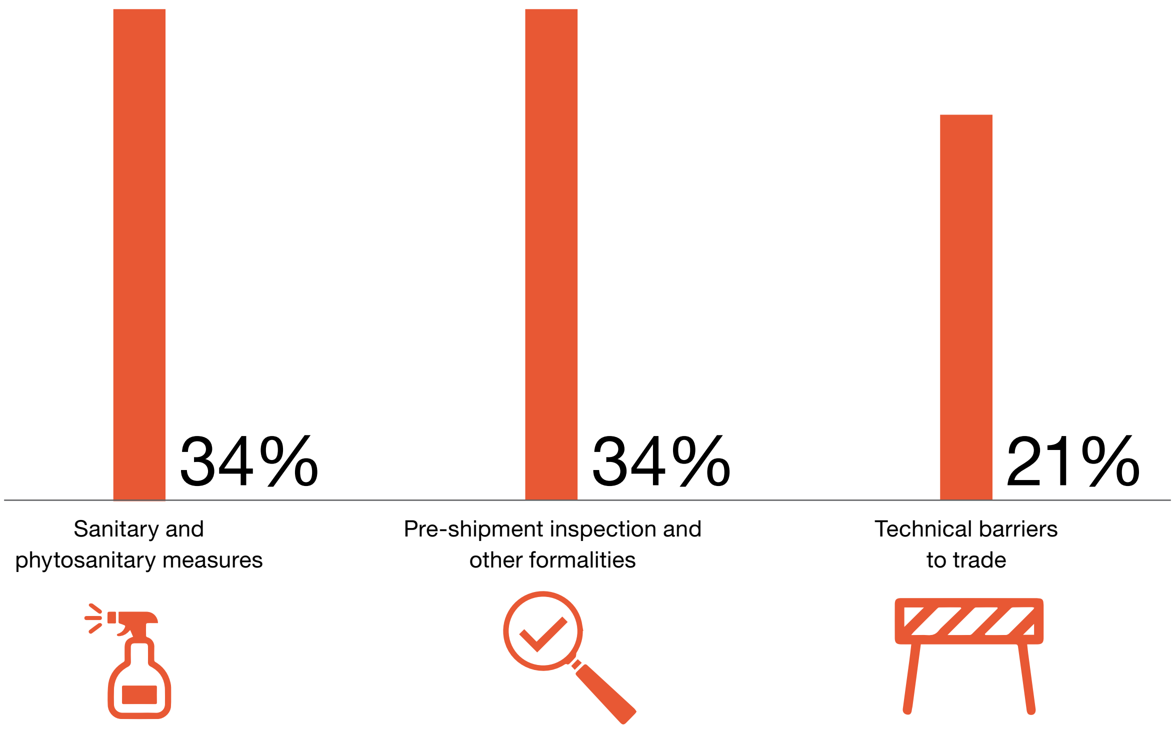
Key impediments to exports



India Inc. finds it challenging to compete with the leading exporting nations mostly in terms of price. It believes that the quantum of incentives extended by competing nations is higher, so the manufacturing sector continues to look for government support to create an enabling ecosystem to provide them with a level playing field.

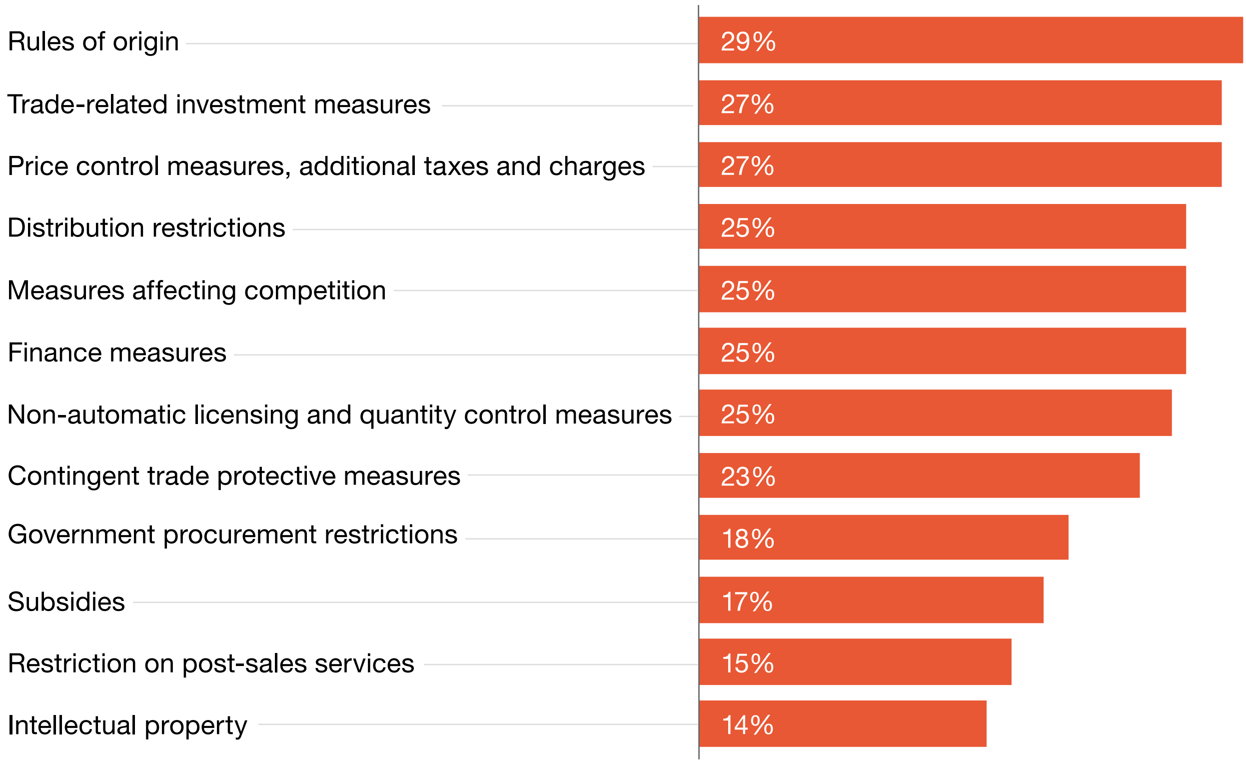
Trading across borders is still a concern for exporters due to measures imposed by importing countries

Among technical measures from importing countries, primary concerns of Indian exporters include sanitary and phytosanitary measures such as certifications, testing procedures; pre-shipment formalities such as customs procedures and pre-shipment inspection; and technical barriers such as quality requirements, labelling regulations and other specifications.



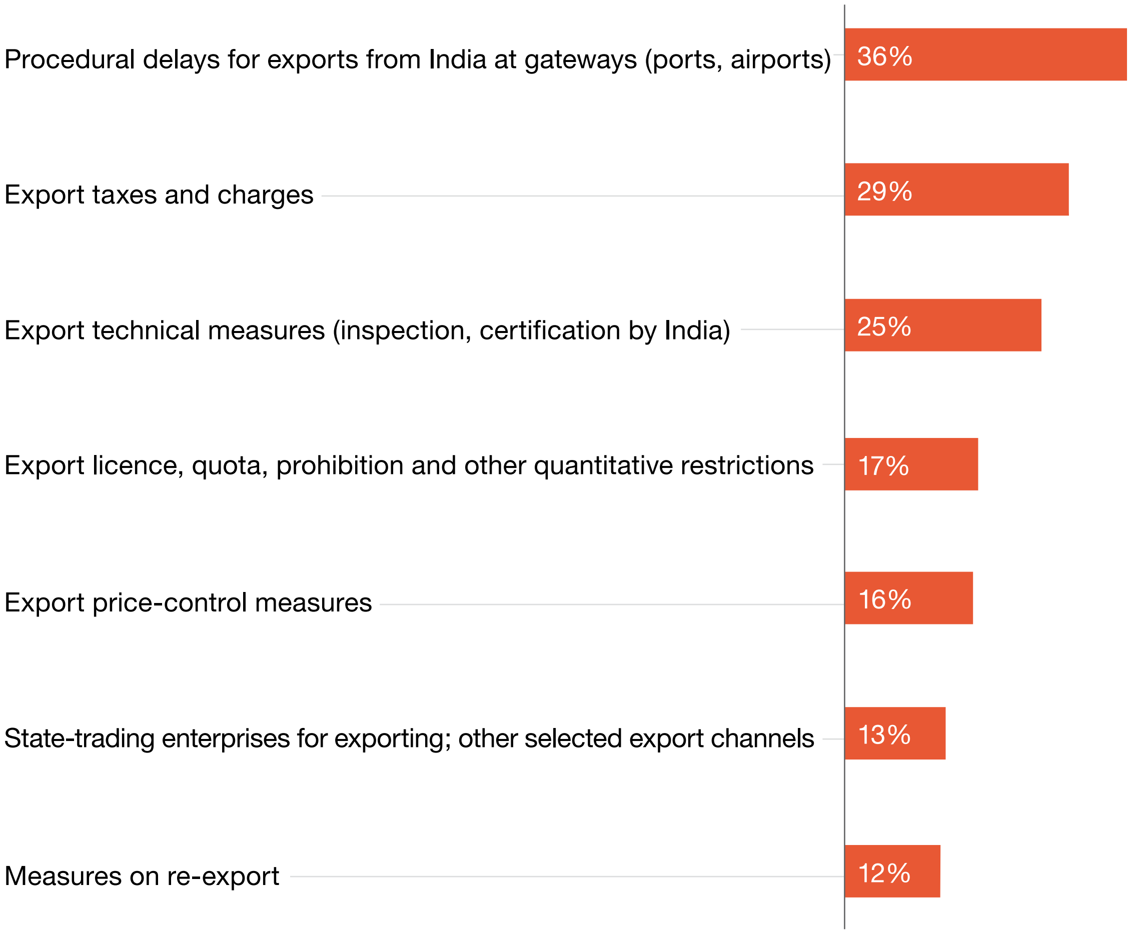
Restrictions imposed by importing countries are limiting export potential

Among non-technical measures hindering exports to destination economies, price control measures (such as administrative measures affecting customs value, seasonal duties, custom surcharges), distribution restrictions (such as limiting sales of goods to certain areas within an importing country, or by designated retailers only) and rules of origin (including measures restricting origin of products or their inputs) are seen as major impediments.



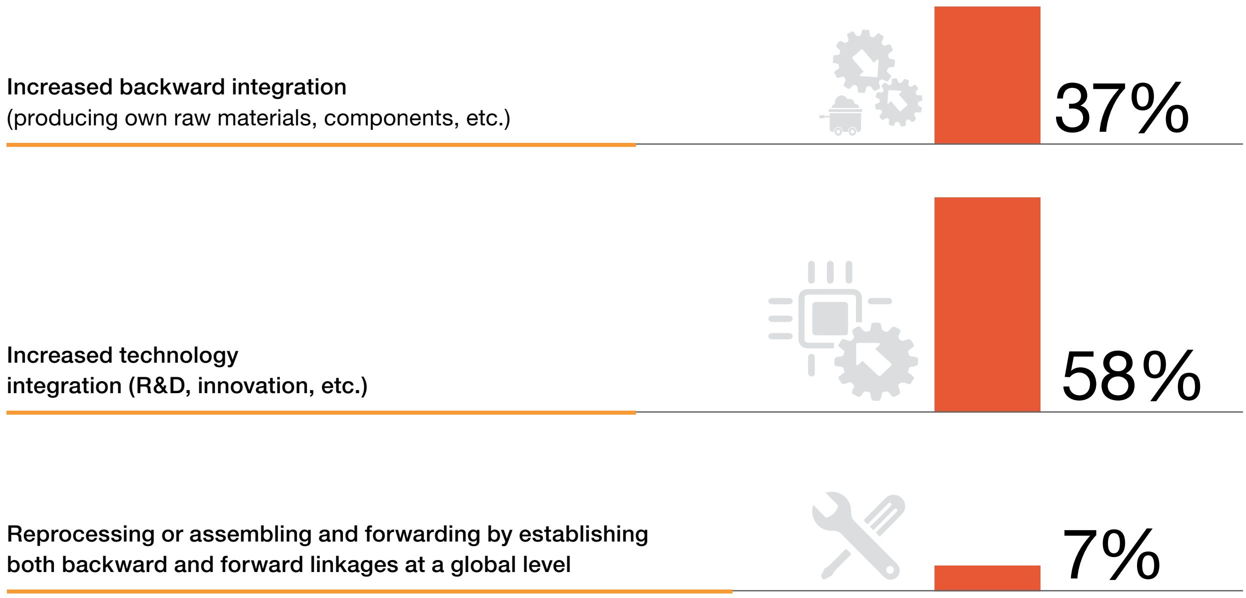
Export-related procedures at gateways are perceived as a major impediment to exports from India

Export-related measures (by India on exported goods)



India Inc. is to focus on technology integration, innovation and backward integration to increase competitiveness

Focus on components of value chain to increase competitiveness



As per the economics of a product value chain, R&D/innovation and component manufacturing add higher value. Thus, a majority of the respondents believe that focusing on higher value-adding activities through technological advancement and backward integration will catalyse India’s movement up the product value chain and enhance export competitiveness.

3 Business leader speak

“ As one of the fastest growing countries, with hopes of lots of investment and jobs to be generated in future, the country is moving in a positive direction.

“ The Indian economy started to gain some real momentum a few years ago when top international companies started to move their manufacturing facilities to India.

“ The rapid pace of innovation and R&D in India due to digitalisation helps in accelerating the future of the Indian economy and its businesses.

“ Being in control of product development and R&D helps in satisfying the wide range of consumer needs which are changing very quickly, and also helps in achieving new opportunities.

“ Increase in the production capacity of manufacturers and increment in the value of exports show that the Indian economy is more stable now and has a strong future ahead.

“ India has taken the necessary steps to make its presence felt in the world economy. The investment outlook in some overseas markets looks positive.

“ Backward integration is a good way to gain more control over production and material supply, market control, and ability to offer competitive prices.

4 Key takeaways

Key takeaways

Indian economy and business conditions

India Inc. is upbeat about the future of the Indian economy as growth is to be driven by strong domestic demand and an increased focus on export markets. Over 7% growth in GDP in the next 12 months looks achievable, and is aligned with the views of institutions such as the World Bank, Asian Development Bank and IMF. Respondents from the focus sectors believe their sectors on an average will witness over 5% incremental growth over the current year's performance.

Key factors driving this confidence include strong public sector driven infrastructure development, easing out of business and regulatory processes, and opening up of FDI in several sectors, including simplification of FDI rules for large investments (e.g. abolition of the Foreign Investment Promotion Board [FIPB] and introduction of a fast-tracking mechanism for FDI cases). In FY 2018, the country received the highest amount of FDI, to the tune of USD 61.9 billion.[4]

The positive sentiment around Indian business conditions is also on account of EoDB reforms that helped the country jump 53 places on the World Bank's 'Doing Business' Index in 2 years.[5] In 2017–18, states and union territories introduced 7,758 reforms. India Inc. expects the Government to maintain the momentum on the on-ground implementation of these state-level EoDB reforms.

Implementation of Goods and Services Tax has also brought in supply chain efficiency and respondents expect the benefits to be more visible over the long term, as the current period is too short to give a clear opinion on the quantum of impact. Investment decisions are now being made based on the supply chain planning and intent to be closer to markets instead of attempting to maximise state tax incentives. Respondents believe that GST will play an important role in increasing the FDI in the manufacturing sector, and 90% are confident that GST will boost their sectoral growth.

Export competitiveness

Currently, over 65% of the companies whose CXOs participated in the survey have the Indian market as their major source of business. However, 85% of them believe that their future growth will be driven by export demand. This is in sync with India's export performance over the last 12 months. In FY 2017–18, India's exports grew by 9.8%, and that was the fastest growth in the last 5 years.

An interesting observation from the survey is around quality advantage being seen as the reason for driving export growth, ahead of cost advantage as the primary reason for exports. However, imports during the same period also grew by 19.6%. As per discussions with CEOs during the survey, non-availability of intermediate products and raw materials and cost and quality advantages in sourcing from other markets were seen as the key reasons for rising imports. But what is encouraging is that most of them believe that over the next 5 years, their dependence on imports will reduce.

To make export growth more sustainable, the industry requires an ecosystem that promotes manufacturing competitiveness and facilitates the production of goods of global quality standards at prices that are competitive. Stronger economic relations with certain countries in target sectors will enable the development of competitive supply chains beyond Indian borders. To promote export growth in terms of operations, India Inc. expects the Government's support in:

- capacity augmentation at export gateways to reduce waiting time
- enhancement of key trade infrastructure at the gateways
- improvement of soft infrastructure through simplification of processes to reduce procedural delays at export gateways and creation of digital platforms

- improvement of manufacturing standardisation and safety procedures – specific government focus on manufacturing standards harmonisation, and development of safety protocols for intermediate and final products to ensure compliance with global standards
- policy measures to aid in ecosystem improvement for the manufacturing industry in India and creating a quality and cost advantage over global competition
- continuous evaluation of existing policies and schemes along with corrective measures to remove rising constraints to manufacturing and exports on account of the changing global and domestic landscape.

4. FDI Statistics, Department of Industrial Policy & Promotion
5. http://www.doingbusiness.org/en/rankings; PwC's India Manufacturing Barometer 2018

5 Methodology

Survey methodology

The PwC–FICCI India Manufacturing Barometer survey was carried out from 6 July 2018–19 October 2018. The profiles of the personnel surveyed included chief executive officers, chief financial officers, chief operating officers and heads of strategy from the Indian manufacturing sector. The survey was jointly undertaken by PwC and FICCI personnel, with the support of a survey agency, by way of face-to-face and telephonic interactions.

A balanced approach was adopted for the selection of survey respondents. They represent a mix of companies engaged in exports with varied technology and human capital requirements. Large as well as medium-scale organisations were included in order to gain a balanced viewpoint on manufacturing and the export competitiveness of India's manufacturing sector. The sample includes companies that contribute approximately 12% to the manufacturing GDP of the country.

For the survey, the following sectors were selected:

- Automobiles and auto components
- Chemicals
- Electrical machinery
- Food processing
- Leather
- Pharmaceuticals
- Textiles

Notes

About PwC

At PwC, our purpose is to build trust in society and solve important problems. We're a network of firms in 158 countries with over 250,000 people who are committed to delivering quality in assurance, advisory and tax services. Find out more and tell us what matters to you by visiting us at www.pwc.com

In India, PwC has offices in these cities: Ahmedabad, Bengaluru, Chennai, Delhi NCR, Hyderabad, Kolkata, Mumbai and Pune. For more information about PwC India's service offerings, visit www.pwc.in

PwC refers to the PwC network and/or one or more of its member firms, each of which is a separate legal entity. Please see www.pwc.com/structure for further details.

About FICCI

Established in 1927, FICCI is the largest and oldest apex business organisation in India. Its history is closely interwoven with India's struggle for independence, its industrialization, and its emergence as one of the most rapidly growing global economies.

A non-government, not-for-profit organisation, FICCI is the voice of India's business and industry. From influencing policy to encouraging debate and engaging with policymakers and civil society, FICCI articulates the views and concerns of industry. It serves its members from the Indian private and public corporate sectors and multinational companies, drawing its strength from diverse regional chambers of commerce and industry across states, and reaching out to over 2,50,000 companies.

FICCI provides a platform for networking and consensus building within and across sectors and is the first port of call for Indian industry, policymakers and the international business community.

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