Manufacturing in India – Pressing the paddle

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Abstract

As the world develops the nations develop, it has always been developing with a tradition of being lead by super powers as USSR, Japan, Germany, USA and many more have lead the other nations. Now the nations at the back seat have taken the control and when we talk about emerging economies of 21st century it starts with two major economy of south East Asia i.e. India and China. While manufacturing in India has remained healthy due to strong domestic demand, its contribution to GDP is only 16%, compared to 34% in China, and largely oriented to the domestic market. This article includes the ambit of its execution of its initiatives and to develop its existing market as well.

Introduction

India's manufacturing quality and engineering skills have improved significantly over the year. Whether we talk about engineered goods, customized products, raw material, pharmacy, software industry or any other, India is escalating in every field. The concerns with China-manufactured products have provided the opportunity for India as well as other developing countries to try and claim some portion of the manufacturing pie from China.

India has made significant progress in the manufacturing sector and has many factors in its favour. However, it faces several serious challenges which hamper the growth of its manufacturing sector. Nonetheless, despite the handicaps, India has been able to achieve remarkable growth in the manufacturing sector in recent years. India has the potential and capacity to become the next manufacturing hub. India is able to further build its reputation in the manufacturing sector in the coming years, the world will soon be asking for Indian-manufactured products. Whilst the Indian manufacturing sector holds great promise, it is perhaps a bit premature to carry the Indian manufacturing flag too high up. There are several critical areas in the manufacturing chain that could derail India's effort to becoming a manufacturing centre, let alone competing and taking over from China in this regard.

The scope of manufacturing in India

The cost of labour in India has remained relatively low. Focusing on the organised manufacturing sector, the US Labour Bureau data show that average hourly compensation costs in India in 2009 were about 25% lower than in China. Nevertheless, Indian manufacturing is surprisingly capital intensive compared to China and Indonesia. In 11 out of 14 manufacturing sub-sectors, India has the highest capital-labour ratio. India has also specialised in more skill-intensive production compared to its peers. India's organised manufacturing has higher capital-intensities than countries at the same level of development and with similar factor endowments. India has emphasized skill-intensive rather than labour-intensive manufacturing, and in terms of productivity skill-intensive sectors stand out. Recent economic growth has benefitted industries which rely more on capital and skilled workers as opposed to low skilled workers.

India should better channel employment from low productivity agriculture to higher productivity manufacturing and services, which would raise wages and living standards for a larger share of the population. Furthermore, India should aim for more formal jobs in the organised manufacturing sector, as these tend to be the most secure and of highest productivity. Indeed, household surveys show that male urban manufacturing workers with regular jobs on average get a salary 2.5 times the level of casual contract workers in the same sector (NSSO, 2011-12). Informality is typically associated with lower productivity and many workers remain outside the reach of labour market regulations and social protection schemes, resulting in higher inequality.

There is little doubt that India has been moving progressively to becoming a competeing manufacturing hub to China and other developing countries. There are several reasons for India's manufacturing competitiveness. The benefit of labour arbitrage continues to provide the basic comparative cost advantage. India's gross domestic product grew by nine percent in the last two (fiscal) years. India grew at six percent in the 1990s, compared to five percent in the 1980s. This large, rapidly growing market will be the key to India's manufacturing base. Companies in India can leverage on this domestic market growth to attain export competitiveness through scaling up capacities. Domestic scale restrictive policies such as the reservation for small-scale industries have been largely removed and are no longer an entry barrier in many labour-intensive industries.

Manufacturing in the ambit of National policy

In the last two decades, Indian economy has witnessed a transformational change and has emerged as one of the fastest growing economies of the world. Industrial development in Independent India was catalysed by three major industrial policy resolutions of Government of India in 1948, 1956 and 1991, which provided a strong industrial base. Economic reforms unveiled in 1991, have brought about a structural shift enabling the private sector to assume a much larger role in all sectors of economy. However, the growth of GDP in India has largely been enabled by a dynamic growth in the services sector. Though in the recent past, the growth of the manufacturing sector has generally outpaced the overall growth rate of the economy, at just over 16 percent of GDP, the contribution of the manufacturing sector in India is much below its potential. This situation is a cause of concern especially when seen in the context of transformation registered in this sector by other Asian countries in similar stages of development. The increasing gap in the sectoral share and the productivity of the manufacturing sector, between India and these economies, indicates that we have not been able to fully leverage the opportunities provided by the dynamics of globalization.

This also has attendant socio economic manifestations in terms of over dependence of a large section of the population on agriculture for its livelihood, disguised unemployment and urban unemployment. India has a favourable demographic profile with over 60% of population in the working age group of 15-59 years. For a country with the largest young population in the world, this creates a challenge of significant magnitude. Over the next decade, India has to create gainful employment opportunities for a large section of its population, with varying degrees of skills and qualifications. This will entail creation of 220 million jobs by 2025 in order to reap the demographic dividend. The manufacturing sector would have to be the bulwark of this employment creation initiative. Every job created in manufacturing has a multiplier effect of creating two to three additional jobs in related activities.

Therefore, a thrust on manufacturing is integral to the inclusive growth agenda of the government. Besides the employment imperative, the development of the manufacturing sector is critical from the point of view of ensuring that the growth model of India is sustainable by providing value addition to our natural and agricultural resources, addressing our strategic needs, and developing new technologies for the welfare of our citizens.

Apart from regulations governing doing business, manufacturing is affected by stringent labour regulations, infrastructure bottlenecks, and the tax system. Policies are needed to address all these issues. Manufacturing growth is constrained by a complex business environment. India ranks 130th jumped 4 places from 134th out of 189 countries in the World Bank Doing Business 2014 data. The Government of India has laid down much emphasize on transforming the basic framework for manufacturing industries and has started an all new platform “Make in India” to welcome foreign investments and to relax the various Complex and strict labour regulations imply large compliance costs and discourage formal job creation.

“MAKE IN INDIA”

The NMP has six objectives:

i) Increase manufacturing sector growth to 12-14% over the medium term, to contribute at least 25% of the National GDP by 2022;
ii) Promote job creation in manufacturing with a target of 100 million additional jobs by 2022;
iii) Create appropriate skills among the rural migrants and urban poor to make growth inclusive;
iv) Increase domestic value addition and technological depth in manufacturing;
v) Enhance global competitiveness of Indian manufacturing;
vi) Ensure sustainability of growth, particularly with regard to the environment.

The NMP provides special focus to industries that are employment intensive, those producing capital goods, those having strategic significance and where India enjoys a competitive advantage (automobile, pharmaceuticals and medical equipment), small and medium enterprises, and public sector enterprises – the so-called Special Focus Sectors.

The NMP stipulates creation of national investment and manufacturing zones (NIMZs), which will be newly set up cities to ensure agglomeration economies, superior infrastructure, lower red tape, flexible labour market regulation and skilled labour.
The broad policy instruments are:
i) Rationalisation and simplification of business regulations;
ii) Simple and expeditious exit mechanism to close sick units while protecting labour interests;
iii) Financial and institutional mechanisms for technology development, including green technologies;
iv) Industrial training and skill up-gradation measures;
v) Incentives for SMEs;
vi) Special Focus Sectors;
vii) Leveraging infrastructure deficit and government procurement - including defence;
viii) Clustering and aggregation through National Investment and Manufacturing Zones (NIMZs);

ix) Trade Policy that does not adversely impact domestic manufacturing.

While the NMP has clear outcome targets, progress up to 2014 has been limited. The implementation of policy reforms to reach these targets has remained a challenge.

On September 2014, Prime Minister Narender Modi announced the "Make in India" campaign to promote the manufacturing sector and spur job creation. The Prime Minister invites foreign companies to invest in India and promises that his government will provide effective and easy governance to help India become a global manufacturing hub. The key objective is to simplify regulations and reporting requirements and ensure more stable policies, including tax policies.

Major highlights of *Make in India*:

- Easing policies and laws: A comprehensive approach is envisaged, including amending labour laws, developing skills, easing FDI policies and up-scaling infrastructure.
- An Invest India team and a dedicated portal for business queries: An investor facilitation team set up by the government will act as the first reference point for guiding foreign investors on all aspects of regulatory and policy issues and to assist them in obtaining regulatory clearances. The information and facts that potential investors need for each sector have been compiled in brochures. A dedicated team has been created to answer queries from companies through a newly created web portal, pledging to answer queries within 72 hours.
- Consolidated services and faster security clearances: All central government services are being integrated into an e-Biz single window online portal. The Ministry of Home Affairs will give all security clearances to investment proposals within 3 months and government departments are asked to streamline approval processes.
- 25 sectors where India can be a world leader have been identified: *Make in India* will focus on creating jobs and enhance skills in these sectors, which include capital goods and engineering, defence equipment, pharmaceuticals, food processing, auto and auto components, textiles and electronics.

Make in India builds on the NMP and is in most respects consistent with it, although it more openly extends a hand to foreign investors.

The Essentials

There is long list of provisions to be considered and fulfilled in the sphere of manufacturing; all these are created by the government. Government change the basic structure or make new formulas to boost the essential areas. NITI Aayog (The institution for planning and transforming India) has identified these as : digitization of land and resource maps and creation of land banks by states; water zoning; offset policy; fiscal and exchange rate measures; strategic acquisitions; development of world class manufacturing management capabilities; trade policy especially boosting India's exports; and reforming the role of public sector enterprises. A lower emission inclusive growth strategy is another important area. These issues may be addressed through separate policy initiatives.

The relatively low level of value-addition in the products manufactured in the country, and the growing imports of capital equipment – the building blocks of a country's manufacturing competitiveness also needs to be addressed urgently. Acquiring depth in manufacturing is crucial from the stand point of long-term competitiveness in strategic areas of economy such as defence and telecommunication. It is important to have a strong indigenous value chain addition element from the stand point of national security.

Finally, the growth of the manufacturing sector has to be made sustainable, particularly ensuring environmental sustainability through green technologies, energy efficiency, and optimal utilization of natural resources and restoration of damaged / degraded eco-systems. Developments of Indian manufacturing sector calls for deepening and recalibrating of economic reforms that would strengthen the sector and make it grow faster and become an engine of inclusive growth.

Bottlenecks

The key obstacle for India is its poor infrastructure, especially in ports and shipping facilities and power. These are important entities and India need to invest significantly in infrastructure. Equally important but perhaps less challenging is the need for India to build the reputation of the “made in India” brand label. The supplier needs to meet the quality standards set by the buyer. India enjoys the reputation of high quality and delivery in the IT and IT-enabled industries (Business Process Outsourcing). However, it needs to set up a large number of product quality testing laboratories to meet environmental and sanitary standards required to sell in the global market. One possibility is to rapidly upgrade university laboratories by encouraging industry-government-university collaborations.

India’s manufacturing sector will be driven by a US$ 500 billion investment in infrastructure across sectors in the near term. Innovation in manufacturing is crucial; India’s competitive edge is not only in labour arbitrage but in technologically intensive manufacturing. Both, a shortage of roads and power and a skills shortage pose challenges to the manufacturing sector.

The manufacturing sector in India faces acute challenges. From problems with power, ports, railroads and roads to a shortage of human capital, manufacturing in India has long lagged behind targeted goals. But the Indian government's commitment to raise its investment in infrastructure from 7% to 9% represents a US$ 500 billion opportunity for growth within India's manufacturing sector. A number of foreign manufacturers have met India’s infrastructure bottlenecks head on, with considerable success. India's own domestic market is large, with over 600 million rural consumers. Workers’ wages in India are less than half of those in China. India has a large talent pool from which to draw, including a strong engineering ecosystem.

From a strategic point of view, growth in the coming decades will come from the developing world. India is in an excellent position to serve emerging economies in Latin America, Africa and elsewhere in Asia. Currently, that represents 11% of India's export market, but it is set to grow dramatically.

India's competitive advantage is in technology-intensive manufacturing. Indian manufacturers must lead by innovation. One challenge facing Indian manufacturing at a time of tremendous growth is high turnover. When the economy grows at a rate beyond 7-8%, companies face a skills shortage and turnover increases from a manageable 2-3% to as much as 20-30%. This creates an unstable environment for manufacturing. The challenge can be mitigated by dramatically increasing the capacity of human resources. Another challenge is public sector control and the requirement that companies bidding on very large infrastructure projects must have previous experience in the field, which many India companies lack. This results in Indian companies losing out in the competitive bidding process to foreign firms. At the same time, state governments have been proactive in making manufacturing zones attractive to automobile and other manufacturers. The Indian government has identified areas where its intervention is required, such as social services, and infrastructure, where private industry is more capable.

Innovation in the modes and models of manufacturing can be a solution to the surplus of India's labour pool, which is largely unskilled but highly entrepreneurial. At the same time, core manufacturing capabilities are important for creating a first-world economy.

Conclusion

The manufacturing sector is the only industry that can make India stand out; it is a massive industry that requires efforts from every direction. It would be difficult for small enterprises to leap out but can change face by optimizing economies of scale. It is also interesting to note that leading international companies have established manufacturing units in India. Similarly, domestic companies have scaled up to meet global requirements.

Many India firms are building up the global supply capability model by accessing the China market for components, acquiring stake in foreign companies to facilitate marketing, servicing, and establishing local assembly and/or manufacturing units abroad. This is a completely new mindset of globalising Indian companies.

India's manufacturing quality and engineering skills have improved significantly over the year. India's gross domestic product grew by nine percent in the last two (fiscal) years. India grew at six percent in the 1990s, compared to five percent in the 1980s. This large, rapidly growing market will be the key to India's manufacturing base.

There have been tremendous efforts to change the face of Indian industry and to make it a single point interaction for investors. India's manufacturing sector could touch US$ 1 trillion by 2025. There is potential for the sector to account for 25-30 per cent of the country's GDP and create up to 90 million domestic jobs by 2025. Business conditions in the Indian manufacturing sector continue to remain positive. With impetus on developing industrial corridors and smart cities, the government aims to ensure holistic development of the nation. The corridors would further assist in integrating, monitoring and creating a conducive environment for the industrial development and will promote advance practices in manufacturing. The continuous efforts and policies of the government is accumulating the energies and potentialities which is directed towards making India a self sufficient and next manufacturing hub of the globe.

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