Defence Industry Facing Survival Issues Due to Regressive FDI Norms

New Delhi, 10 May, 2014: FICCI has been strongly advocating policy regimes that facilitate building a strong Defence Industry in India. Towards this FICCI has supports defence industry's apprehensions on the serious implications of Consolidated FDI Policy Circular of 2014 (effective from April 17, 2014) issued by Department of Industrial Policy and Promotion on the continuance of Indian conglomerates, both Public as well as Private, in the defence business.

While FICCI has welcomed periodic revision in FDI policies to keep pace with economic scenario of the country, in a formal communication addressed to Secretary DIPP, FICCI has pointed out the survival issues the policy circular has caused for the sector. With MoD now getting committed to indigenising the sector, the DIPP circular freezing FII holding as on 22ndAug 2013 in Defence Licensee companies heralds roadblocks in the process the government has embarked in the recent past.

FICCI has argued that a blanket ban on Investment by Foreign Portfolio Investors FDIs/FIIs in listed Indian conglomerates, where defence business is just one of the business verticals will not be a practical view in the current corporate as well as regulatory structure.

Dr. A Didar Singh, Secretary General , FICCI said " With the implementation of this circular, no listed companies will be able to continue its defence business as it will be impractical to stop FII's to invest in large conglomerates or group holding companies. It is not feasible for any corporate to stop active trading of their stock on recognised stock exchanges as long as the portfolio investments are within limits defined under Schedule 2 of the Portfolio Investment Scheme, under holding prescribed under Schedule 2 of the FEMA regulations. The only option for the corporates is either close the defence business or de-list from the stock exchanges. Both the solutions do not seem to be warranted in the interest of vibrant defence industrial base in country."

FICCI believes that the policy seem to have been inadvertently applied the norms meant for control and governing of the Defence joint venture companies specifically created by Indian Industrial houses, either private or public, to the parent companies, widely held by Indian public and Financial Institutions. FICCI would like to point out that the norms meant for such specifically created Joint Venture companies certainly need to consider the FDI and FII ownership together and be capped within the sectoral caps, defined from time to time.
FICCI has further argued that the intent of the policy should be to exercise "control" over a strategic sector like defence while leaving the ownership subject to the current guidelines under RBI and FEMA.

The table below shows various share holding patterns in some large and stock exchange listed companies. The shareholding pattern of large private companies and conglomerates will not be able to meet the 51% shareholding clause.

Description	BEL (%)	Pvt Sector Company with Promoter Holding (%)	BEML (%)	Widely Held Pvt sector Company without Promoter holding (%)
Promoters	75.86	31.81	54.03	0.00
Individuals	1.87	15.42	6.27	23.96
Institutions	15.93	26.53	26.40	36.63
FII	3.83	21.87	7.63	15.62
Govt.	0.00	0.03	0.00	0.00
Others	2.51	4.34	5.67	23.79

Such restrictions on FII/FPI flows may repeal large and widely held conglomerates who have acquired niche capabilities in defence over the last decade, reconsider their continuation in this strategic sector. Also during renewal of licences, the companies need to provide information on shareholding pattern. It is well known that FII investments are never static and keeps changing with market conditions on day to day basis.

The above mentioned policy circular will thus lead to increase in imports of defence hardware and go against the strategy of attaining substantive self reliance, development of an indigenous technology and Industrial base and preference to indigenous procurement that Ministry of Defence has been championing under the DPP 2013.

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