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● GLOBAL SUPPLY CHAIN

Eyeing an Indian iPhone

“Made in country x” has become a misnomer as ‘x’ would involve large number of countries, and different locations could have a share in the final value added

IN A HYPER-GLOBALISED world emergence of global supply chains occupies a key role. Apart from innovation and design, success of various products could be traced in the design of successful supply chain strategy of the multinational corporations. Apple iPhone serves as a good example. Apple purchases components from various suppliers spread all over the world, and then gets these shipped to the assembling plant in China—the finished product then is shipped to Apple’s stores and online channels all over the world.

In this story, a key element is emergence of China as a worldwide hub of the global supply chain. Various factors could have contributed to China’s emergence as a manufacturing and trade giant—inexpensive labour, steadily reducing tariffs, presence of effective special economic zones, easy availability of land, artificially manipulated exchange rate, or scanty regard for intellectual property rights. Are some of these narratives changing with the on-going trade war between the US and China? Are some of the “made in China” efforts looking for newer desti-

nations? Are these part of the risk diversification strategy of the global players?

While firm data is yet to emerge, some specific instances could be illustrative. Recently, Samsung exited its smartphone assembly operations in China by closing its last assembly unit in Guangdong. Also, Apple’s smartphone market share in China has emerged highly competitive due to the strong presence of the local players. Globally, Apple is wrestling with the future of iPhone’s capability to keep pace with the high expectations of product innovation in smartphone category. The newly acquired momentum with iPhone 11 series may not be sustainable given the overall competitiveness and commoditisation of incremental innovations. There are media reports in mid-2019 that Apple has started exploring moving some part of its hardware production out of China and has asked its key manufacturing partners like Foxconn, Pegatron, and Wistron to evaluate the available options. In particular, Apple has relocated some of its manufacturing bases to India as a source of regaining competitive advantage in the form of lower

wages in the assembly of iPhones. The recent phenomenon of Apple assembling one of the high-end models, Apple iPhone XR, in Chennai’s unit of Foxconn is perhaps a building block to this new emerging narrative. Admittedly, even before Foxconn, Taiwan’s Wistron had started iPhone assembly in India near Bengaluru in 2017; it was, however, limited to older models. The current relocation to Chennai has huge implications for the smartphone manufacturing supply chain capabilities in India.

Both push and pull factors could be operative here. In terms of the push factors, with the wages in China increasing, and threats of trade war looming large, China could be in the process of becoming less attractive in the days to come. In such a situation, countries like Vietnam or India, which over the years, have improved their attractiveness as business destinations, would be the beneficiaries.

Notwithstanding concerns over India’s infrastructure, its rank in World Bank’s ease of doing business has experienced a quantum leap—from 130 in 2017 to 77 in 2019. Similarly, while the proportion of formally skilled workers is much lower, in comparison with China, India’s burgeoning services sector and significant number of high-skilled graduates related to information technology could give comfort to the multinational corporations, like Apple, to relocate their base. The recent cut in corporate tax rates could also act as an incentive.

Is this illustration of Apple relocating its production base to India going to be part of a trend or a one-off phenomenon? Two issues can be highlighted. First, there is a general lull in the attractiveness of the emerging market economies in terms of pulling foreign direct investment (FDI) in recent times. As per the AT Kearney Foreign Direct Investment Confidence Index, India has slipped from 8th position to 16th position from 2017 to 2019, China too has glided from the third position to 7th position during this period. In fact, the report highlights the role of “multi-localism” as a driving force behind determining FDI destinations. Second, there is a constant threat from comparator economies. Illustratively, what gets relocated to India today may well get relocated to Vietnam tomorrow, unless we are able to maintain our comparative advantage. After all, the gains from trade and investment are inherently dynamic in nature.

However, one should be cautious of any rash optimism or expectations of

emergence of a goldilocks scenario. It would be an uphill task for technology firms to replicate the incumbent capabilities and advantages of an ecosystem offered by China. Foxconn had a monumental advantage of process differentiation in China in the form of volume flexibility of ramp-up and ramp-down, tooling and engineering capabilities at lower cost, stable component supplier base, among others. While the narrative now shifts to countries like India and aligns with the strategic policy framework of Make-in-India, it would not be easy to replicate the robustness of ecosystem in China and leverage those benefits immediately. The components for assembly of iPhone XR are still largely imported and may not significantly provide cost advantage in the short run. The real dividend for Make-in-India would be when the value creation in the supply chain is enhanced. The upstream supply chain should be replicated in the form of component manufacturing that would have the real cost reduction potential. It is well-understood that in sustainable business models, process innovations often trump over product innovations. After all, with so much of competition in the product innovation in smartphone category, the real differentiator is the process design of the supply chain, and Apple has a long journey towards this end in manufacturing bases like India. Besides, potential competition from countries like Vietnam looms large. Interestingly, a recent report of the UNCTAD on “Trade and trade diversion effects of United States tariffs on China” revealed that out of an estimated \$35 billion loss in Chinese exports due to the trade war, about \$21 billion (63%) were diverted to other countries. While India gained about \$755 million in additional exports, mainly of chemicals, metals and ore, the extent of gain was much more in case of countries like Mexico (\$3.5 billion), or Vietnam (\$2.6 billion).

In the twenty-first century, globalisation is synonymous to emergence of global supply chains. “Made in country x” has become a misnomer as ‘x’ would involve large number of countries, and different locations could have a share in the final value added. In a lighter vein, thus, any hope of treating the “i” in “iPhone” as representative of “India” could be premature. But notwithstanding such dampeners and caveats, the news of iPhones being made in India is indeed a welcome development particularly at a time when amidst the current slowdown we are in look out for some silver lining.

Contract ready

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Avantis Regtech, a TeamLease company. Views are personal



Government must lead by example and respect the contracts it enters into

APARKING DISPUTE ON November 2, led to a face-off between Delhi lawyers and the police. Work in District courts came to a standstill for more than a week. The standoff between two pillars of law and order on the streets of the capital without any speedy mediation or resolution explains why India is still a difficult place to do business. It is not surprising that despite a significant rise in rank over the past six years in the Ease of Doing Business study (from 142 to 63), the category we still lag dreadfully behind is contract enforcement—India ranks 163 out of 190 countries, up just 20 ranks from 186 in 2015.

Under this head, the time and cost to resolve a commercial dispute and the quality of judicial processes for men and women are measured. The number of days to resolve a commercial dispute in India stands at 1,445, and the quality of judicial process index is rated at a low 10.5 out of 18. China, on the other hand, ranks fifth, with a quality of judicial index score of 16.5 and resolution of a commercial dispute taking 496 days.

The government has tried to make some headway by setting up the NJDG, enacting the Commercial Courts Act etc. However, in a national MSME survey by PHDC and DSE early this year, when asked whether the contracts entered into are easily enforceable now, just 21% felt there has been an improvement, 34% respondents remained neutral, and 44% of the respondents disagreed. While around 40% felt that the time and cost of enforcement in court has reduced significantly, the majority felt otherwise.

It is also telling that the government stands out by not abiding by its own contracts - more than 60% of the 2,861 applications pending on the MSME payments grievance portal against Central and State governments and departments have remained unaddressed for more than 90 days. The government also forms the biggest litigant block in the country. As the first step, the government has to lead by example, respect the contracts it enters into and refrain from clogging the courts and tribunals with infructuous petty cases and appeals. A massive

overhaul of the judicial process obviously needed but is unlikely even in the medium term. Penalty is high—a third of the cases are pending more than three years, more than 6,000 vacancies in judiciary, sanctioned posts have to increase from the present 19 judges per million to 50 as per the Law Commission 1987. Yet, even in the short term, some improvements can be effected when seen through the Ease of Doing Business lens - processes can be rationalised, digitised and simplified to make it easier to file and quicker to resolve commercial

cases. One long overdue measure is the digitisation of all courts to enable online filing of initial complaints and electronic payment of court fees.

Most countries have been working towards setting time standards for disposal of cases. China has regulated the maximum number of adjournments, to be overridden in exceptional circumstances. While the Commercial Courts Act has set strict timelines for the decision after the hearing, an upper limit of a year or two must include execution of the decisions, appeals and final disposal of commercial disputes.

Some issues need deeper intervention. For instance, Alternative Dispute Resolution was introduced way back in 1999 with an amendment to the CPC under Section 89, that gave the judiciary powers to refer cases for out of court settlements. Though civil cases are almost always now pushed towards mediation, twenty years on, India still lacks strength in effective mediators, creating a backlog.

With an eye on improving the EoDB and making India a centre for international commercial arbitrations, the Arbitration and Conciliation (Amendment) Act, 2019 was passed in August. However, it has run into a muddle, with three petitions in the SC contending that Section 87 of the Act is in conflict with the Insolvency and Bankruptcy Code 2016. (FE, Nov 8).

The Economic Survey 2017-18 had pegged Timely Justice as the next frontier for EoDB, recommending coordinated action between the government and judiciary as the key policy solution. In its quest to reach the top 25 in the World Bank ranking, India may find it quicker to move ahead in other parameters. When it comes to contract enforcement, the challenges are deeply rooted.

● **In its quest to reach the top 25 in EoDB ranking, India may find it quicker to move ahead in other parameters, for contract enforcement, the challenges are deeply rooted**

CHATRASAL IN A remarked that “The renewables sector in India is near-death. Capacity addition has markedly slowed down in this financial year. Few projects are achieving financial closure, and so, few projects are getting complete.” (bit.ly/3411JQr, FE, Nov 15, 2017)

The renewable energy (RE) growth momentum lasted into 2018, driven by solar power, but since then the sector has degenerated. While capacity addition in RE was impressive during FY17 (11.3 GW) and FY18 (11.8 GW), there has been a decline in capacity installation (~8.5 GW) during FY19. Performance in rooftop solar has been disappointing—out of a target of 40 GW by 2022, India has been able to achieve 2.1 GW. These lower and slowing increments cumulatively call to question the 175 GW target for 2022 (capacity addition was 83 GW till September 2019).

India has set ambitious targets for renewable energy capacity. The MNRE has further upscaled the 175 GW target of 2022 to 227 GW. Moreover, the PM at a recent UN Climate Action Summit suggested an even higher potential uptick to 450 GW.

Power tariffs had declined significantly in 2016-17, ensuring price competitiveness. However, since then, RE sector risks have increased. Reverse auctions with unviable tariff caps, uncertainty in the applicability of taxes, outstanding dues from discoms (and PPAs risk), have resulted in an insufficient interest from IPPs for solar ten-

Return to growth

Given the mismatch between tariffs and risks, few new renewable IPPs are being created

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ders, resulting in lower capacity addition.

The wind energy sector (in stress since auctions were introduced in February 2017), has seen capacity addition fall from 5.5 GW in FY 17 to 1.86 GW in FY18, and further to 1.5 GW in FY19. The necessarily domestic wind industry simply cannot deliver at the capital costs commensurate with the expected tariffs. No wonder, the October 1.2 GW NTPC tender with a ceiling tariff of ₹2.93/kwh closed without a single bid.

It is debatable what purpose the tariff cap serves as buyers have been cancelling bids. Even the benefit of price discovery is not achieved, when the capital costs are transparent and known to regulators, utility buyers, and PSUs, who are no longer investing (given poor economics). This cap is a severe

distortion of the market, and if the utilities cannot bear higher tariffs, it would be better to let the market decline for commercial reasons till the power demand picks up. Alternatively, the price cap can surely become a FIT, to lead to the same result.

Given the mismatch between tariffs and risks, few new independent power producers (IPPs) are being created, leaving the consolidated sector devoid of MSMEs.

Distributed renewable energy, primarily RTS, has also witnessed slow progress, running at 5% of target. Increasing policy uncertainty, delays in net metering approvals, push-backs by discoms, proposing wheeling charges and power injections caps, and lack of appropriate financing instruments, have resulted in slow uptake.



A report by Crisil concluded that the country is likely to miss the lowest renewable energy target of 175 GW by 2022 by a wide margin of 42% due to regulatory challenges, policy flip-flops and a steep fall in tariffs. The report notes that 26% of the 64 GW of projects auctioned have received no or lukewarm bids, while another 31% are facing delays in allocation after being tendered. The MNRE, however, has rebutted the Crisil report, calling it ‘ill-founded,’ factually incorrect and lacking credibility.

To bridge the gap between these different views, a group of NGOs recently got together to brainstorm ways to revive growth. Their suggestions included:

● Tendering only after all procedural steps are taken, i.e. tariff approval by the

CERC and the state regulatory authority in advance (as far as possible), and signing of PPAs only after full regulatory approvals.

● To learn from MP’s successful rooftop solar bids, where project documentation gave a lot of comfort to bidders and tendering was successful.

● Strict guidelines to states participating in SECI tenders not to re-open PPAs

● Sanctity of the ceiling and an economic rationale for current pricing

● The GOI can commission a study on the composition of delivered tariffs in China and for recently-commissioned plants in India, as it used to be done for the fixed-ROE FITs. This study will show the kind of prices Indian utilities will have to pay for future wind projects. Irrational bidding in the past

by developers/IPPs would no longer be the basis of a price cap once actual capital and financing costs have been identified.

● An alternative to reviving the bidding market: arriving at a benchmark price for every bid instead of setting a price cap.

If the bid price is the only criteria, then the projects would only come up with high-resourced states. Can other states, to create jobs and investments, add other parameters to reward in-state power generation? Can there be multiplicity of competing norms?

Consistency in open access policies: exemptions for open access charges in some states are only for a decade.

For rooftop solar, issues out of NDFCs in net-metering need to be sorted out. NBFCs to appraise small-ticket transactions at low-cost should be fast-tracked.

Consultation with lenders as to why they are not increasing their exposure to RE generation.

RPO enforcement pressure to be kept up to create regulatory demand.

Standard bid documents to be created and kept unchanged for 5 years or more.

A dynamic, sunrise industry growing without subsidies, but in dire need of regulatory support, could benefit from a greater and transparent dialogue among the stakeholders. Denying the slowdown or ignoring the widening gaps between targets and achievements serves no purpose. Some of these suggestions can be debated and implemented to bring back growth in the industry.