India’s FDI Flows

Why in news?

In FY23, India received lower Foreign Direct Investment (FDI) equity inflows than FY22 which raises the situation to analyse India’s FDI status.

What is Foreign Direct Investment (FDI)?

- **FDI** - It is a type of *cross-border investment* in which an investor from one country establishes a lasting interest in an enterprise in another country.
- FDI remains vital for bolstering domestic industry, stimulating growth, and enhancing global competitiveness.
- **Investments under the Automatic route**
    - It require *no prior permission*, resulting in minimal monitoring.
    - It only require the investor to inform the *Reserve Bank of India (RBI)* after the investment is made.
    - FDI up to 100%, under the automatic route is permitted for agriculture, manufacturing, airports, e-commerce, pharmaceuticals, and railway infrastructure.
- **Investments under the Government route**
    - Prior to investment, approval from the Government of India is required.
    - It is permitted in sectors like defense & telecom (beyond 49%), mining (100%) and print media (26%).
- **Security clearances**
    - It apply only to specific areas such as broadcasting, defense, private security, civil aviation, and mining.
    - *Ministry of Home Affairs (MHA) and Ministry of External Affairs (MEA)* overseeing scrutiny and security clearance.

Status of India’s FDI

- **Total FDI** - In terms of market value, the FDI amounted to Rs 50 lakh crore in FY23.
- **Inward FDI** – *The USA* was the largest source of inward FDI followed by Mauritius, the UK and Singapore which collectively accounted for 60% of the inward FDI in the country.
- **Outward FDI** - *Singapore* was the largest beneficiary of outward direct investment (ODI) by Indian firms.
- **Sector wise** - The *manufacturing sector* continued to attract the largest share of FDI equity, both at market value as well as at face value.
- **Services** - Among services, *information & communication and financial & insurance*

activities were the major FDI recipient sectors.
- **Ratio of inward to outward DI** - In terms of market value, ODI growth outpaced the growth in FDI and, as a result, the ratio of inward to outward DI stood at 5.5 times in March 2023.

Source*- RBI's Census on Foreign Liabilities and Assets of Indian Direct Investment Entities*

What are the contemporary issues in FDI inflow?

- **Decline in FDI inflows –** It is due to
  - Spill over of the COVID-19 pandemic
  - Global headwinds such as the Russia-Ukraine conflict and global recessionary pressures
- **Regional disparities in FDI -** The skewed distribution of FDI over the years hamper the development and competitiveness of States.
- The Southern and Western States of Gujarat, Maharashtra, Tamil Nadu, and Karnataka boast more favourable investment environments compared to their northern counterparts.

> *In 2023, the top 5 States attracting FDI include Maharashtra, Karnataka, Gujarat, Delhi, and Tamil Nadu.*

- **Lack of clarity-** FDI Policy 2020 required government approval when the beneficial owner investing in India belonged to any of the 7 neighbouring countries.
- However, a clear definition of a '*beneficial owner*' is missing in the FDI Policy and causes ambiguity to both domestic firms as well as foreign investors.
- **Lesser FDI in Greenfield projects –** *Higher FDI in brownfield* projects doesn't substantially boost employment or capacity as compared to Greenfield enterprises.
- **Transfer of ownership** – FDI at times leads to ownership transfer from Indian companies to foreign entities.
- **Reverse repatriations and outflows** – They are also quite sizable.
- **Risk of exploitation** – Dependence on foreign solutions increases the risk of exploitation underscoring the need for proactive security measures.

Can India rebound its investment potential?

According to the *2023 Economic Survey*, a rebound in incoming FDI is expected due to various factors like

- Sectoral production-linked incentive (PLI) schemes
- Growth prospects in tier-2 and tier-3 cities
- New investment facilitation measures like the *National Single-Window System (NSWS)*
- High-tech industrial development
- Higher market size owing to larger population

- Advancements in the digital and technology ecosystem

- **Foreign Investment Facilitation Portal (FIFP), 2017 -** It *replaced Foreign Investment Promotion Board (FIPB)* for faster processing via approval route.
- **Consolidated FDI Policy 2020 -** Amendment to this policy aimed to prevent opportunistic takeovers of weakened domestic companies by foreign firms during the Covid-19 pandemic.
- It stated that countries sharing land borders with India could no longer invest under the automatic route and must seek approval for proposed investments.

India's neighbouring countries are China, Bangladesh, Pakistan, Bhutan, Nepal, Myanmar, and Afghanistan.

What lies ahead?

- **Focus on Greenfield activities** – Increase FDI in high-tech Greenfield activities which helps in capacity building, managerial improvement and skill development in India.
- **Transparent regulatory framework** – An impartial, uniform screening mechanism for investment promotion and investment protection need to be developed.
- **Independent body for monitoring investments** – It will recognise risk parameters

and nation’s long-term interest while monitoring FDI inflows.

- **Holistic economic approach** – It is needed to balance the nation’s domestic potential and resilience with economic interests without explicitly hampering the interest of the foreign investors.

References

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2. India Briefing| India’s FDI in 2023
3. RBI | Census on Foreign Liabilities and Assets of Indian Direct Investment Entities