Sustaining FDI Inflows

This editorial is based on “How to Sustain the Post-Covid Surge in FDI Inflows” which was published in The Hindu BusinessLine on 22/05/2022. It talks about the significance of the growth of FDIs in India and how can India sustain this growth.

For Prelims: World Investment Report, Foreign Direct Investment (FDI), Make in India, Atmanirbhar Bharat, FPI

For Mains: FDI - Significance, FDI v/s FPI, Measures of sustain surge in FDI inflows

Despite the major slowdown in the global economy induced by the Covid-19 pandemic and the projections of the **World Investment Report** of expected decline in **Foreign Direct Investment (FDI)** flows of 30-40%, the resilient **Asian economies witnessed favourable FDI flows** which were rather **higher than the global average**.

Additionally, **South Asia experienced a robust surge** in FDI during this period, with **India seeing a 27% rise**. Judicious and quick policy initiatives will facilitate more foreign investments and in-turn enhance **India’s potential as a global manufacturing hub**.

What do We know about FDI?

- A Foreign Direct Investment (FDI) is an investment made by a firm or individual in one country into business interests located in another country. FDI **lets an investor purchase a direct business interest in a foreign country**.
  - Investors can make FDI in a number of ways. Some common ones include **establishing a subsidiary** in another country, **acquiring or merging** with an existing foreign company, or **starting a joint venture partnership** with a foreign company.
- Apart from being a critical driver of economic growth, FDI has been a **major non-debt financial resource for the economic development** of India.
  - The Government of India has taken many initiatives in recent years such as **relaxing FDI norms across sectors such as defence**, PSU oil refineries, telecom, power exchanges, and stock exchanges, among others.

What is the Growth Rate Scenario of FDI Inflows to India?

- An analysis of the recent trends in FDI flows at the global level and across regions/countries suggests that **India has generally attracted higher FDI flows** and **continued to remain among the top attractive destinations** for international investors in line with its **gradual liberalisation of the FDI policy** as part of the cautious capital account liberalisation process.
- In 2017-18, the **inflows surpassed $60 billion for the first time ever** and the Department of

Promotion of Industry and Internal Trade (DPIIT) put FDI growth at **14% in 2019-20**, the highest in four years.
    - In 2021, the **total FDI inflow in 2020-21 was $81.7 billion,** up 10% over the previous fiscal.
    - The FDI in the **FY 2021-22 has touched a "highest ever" figure** of $83.57 billion.
- Corporate giants like Silver Lake, Google, Facebook, Foxconn, Saudi Arabia's PIF, General Atlantic Singapore, Hitachi, Walmart and Catterton are **expected to invest billions of dollars in the Indian economy**.

What Factors have Facilitated Higher FDI Inflows?

- **'Make in India'** and **'Atmanirbhar Bharat'** campaigns coupled with strengthening of **India's footing in global supply chains** have given momentum to FDI inflows over the past few years.
- The first wave of the Covid-19 pandemic prompted around 1,000 **companies to shift their base out of China,** with nearly 300 of them being in the areas of medical and electronic devices, mobiles and textiles.
    - For India, companies like Lava International with over 600 employees clarified its intention to shift its base to India from China.
- In most sectors of the economy, **India has one of the most liberalised FDI laws** in the world, allowing foreign **investments of up to** 100% through the automatic method.
    - In its FDI policy, **India has taken a negative list approach,** stating only those sectors and activities where foreign investment is regulated, whereas sectors not named in the document are open to obtaining 100% FDI under the automatic method.
- Higher FDI inflows have been possible due to the **liberal and attractive policy regime for the investors,** a good business climate and reduced regulatory framework.

What will be the Impact of these FDI Inflows?

- Considering the impact of the recent surge in the FDI inflows on macroeconomic variables, there will be an **estimated increase of 5.68% in India's GDP**.
- The **industrial output of sectors like metals, construction,** machinery and equipment, motor vehicle parts, computer, electronics, and optical products are expected to receive a **huge boost relative to others**.
- **Exports are also expected to witness a rise,** because of the FDI-fuelled increase in scale, **quality standards and technology transfer,** along with **enhanced employment opportunities**.

How can India Retain this Growth?

- **Government policies/decisions are of crucial importance** in creating a conducive environment for global investors. The disruptions induced by the pandemic have given opportunities for India to expand its global footprints.
    - The government is striving to strengthen the FDI environment through an array of policy initiatives and reforms at all levels.
    - This also has to be complemented by a **sound trade policy to boost exports** further, encourage **inclusive development,** and **incentivise R&D** (research & development) to make our industry **globally competitive**.
- FDIs have more potential to facilitate the growth of the Indian economy than **Foreign Portfolio Investment (FPI)**. It should be ensured that **India remains an attractive, safe, predictable destination** for serious, long term investors.
    - A level playing field is necessary if we want continued foreign investments. Sneaking loyalty towards local players should be avoided.

What should be the Main Areas of Focus?

- **Concentration to a Few States:** FDI has been concentrated in a few Indian states. The **rapidly growing states receive 60-70% of FDI inflows** into India: Andhra Pradesh, Delhi, Karnataka, Maharashtra, and Tamil Nadu. Even among these states, there is **considerable heterogeneity**.

- It is also these very states that are most successful in converting FDI approvals into actual inflows.
- Bringing other states into the ambit of FDI inflows should be one of the key focus areas.

- **Role of States:** The **federal structure in India** empowers the **states to design their own investment policies to attract FDI,** along with instituting specific incentives for certain sectors.
  - For instance, **Karnataka** has been aggressive in attracting FDI and has outlined a series of policies, such as **investment subsidies, exemptions for export-oriented units,** and refunds and **fiscal incentives for specific industries** such as IT, biotechnology, and business process outsourcing.
  - Example of Karnataka can be emulated by other states.
- **Equally Focussing Other Important Factors:** The other important factors influencing FDI into India are **broader economic policies** including **corporate taxes**, **trade openness**, and other **business climate issues**.
  - India's progress of liberalising its FDI regime is a necessary but not a sufficient condition to attract significant FDI inflows.
  - With the current international attention on India's tremendous potential for FDI, it would be an **opportune time to push for rapid progress on structural reforms** to tremendously increase FDI inflows.

Drishti Mains Question

"The FDI inflows to India in the FY 2021-22 touched a "highest ever" figure of $83.57 billion." Discuss the measures that India can take to sustain this surge in the FDI inflows.

UPSC Civil Services Examination, Previous Year Questions (PYQs)

Q. With reference to Foreign Direct Investment in India, which one of the following is considered its major characteristic? (2020)

(a) It is the investment through capital instruments essentially in a listed company.

(b) It is a largely non-debt creating capital flow.

(c) It is the investment which involves debt-servicing.

(d) It is the investment made by foreign institutional investors in the Government securities.

Ans: (b)