FDI IN INDIA: UNFINISHED AGENDA

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DETERMINANTS OF FDI

Theories: Market Inferfection Hypothesis (Hymer, 1976, Kindleberger, 1969), Location specific Advantages (Franko, 1971 and Vernon, 1977),Internalisation Theory (Buckley and Casson, 1976;Rugman 1986), Eclectic Approach (Dunning, 1988)

Economic Conditions: (1) Market Size, potential market size, Rate of return, Urbanisation/industrialization, Labour cost, human capital, Physical Infrastructure, macroeconomic fundamentals like inflation, financial health, tax regime, macroeconomicstability.

Host Country Policies: Promotion of private ownership, efficient financial market, trade policies/regional trade agreements, FDI policies/investment incentives, legal framework, quality of beaurocarcy and openness

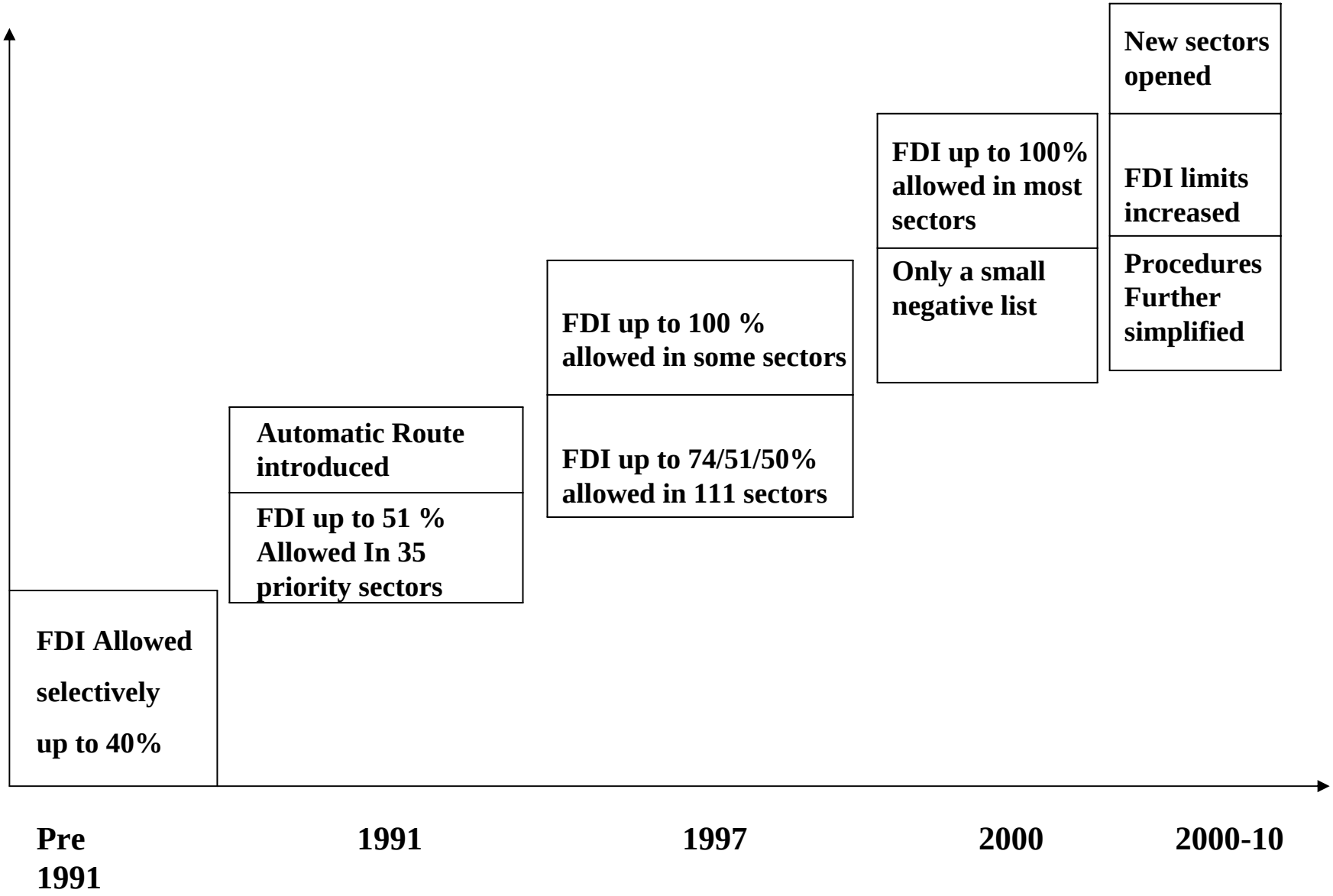
Pre-reforms Period: 1947 to 1991

- Independence to late sixties
- Restrictive policy between late sixties to late seventies
- Relaxed policies of eighties
- Overall FDI policy till 1991.

Post Reforms Period:1991-10

- Efforts to attract non-debt creating capital
- Dismantling control regimes in many areas
- Opening many sectors with hiked equity caps and automatic routes
- Privatisation of public sector
- Abolition of rigid conditions for FDI firms such as high local content, dividend balancing etc.
- Institutional set up for facilitating FDI (FIPB, FIIA, SIA)
- Aggressive signing of BITs and DTTs and Laws to protect IPRs
- Incentives to foreign investment

Liberalization of FDI Policy in India



Major Institutional reforms to Promote FDI

- **Foreign Investment Promotion Board (FIPB):**
  - Foreign Investment Promotion Council (FIPC)
- **Secretariat for Industrial Assistance (SIA):**
  - Entrepreneurial Assistance (EA) unit
  - Investment Promotion and Infrastructure Development (IP&ID)
- **Foreign Investment Implementation Authority (FIIA):**
  - Fast Track Committee
  - Project Monitoring Wing (PMW)

Foreign Investment Policy

Automatic / Government approval route

Special economic Zones and Specialised parks

Repatriation of Investment Capital

Labour laws and regulations

Policy regarding intellectual property rights

Taxation policy and tax incentives

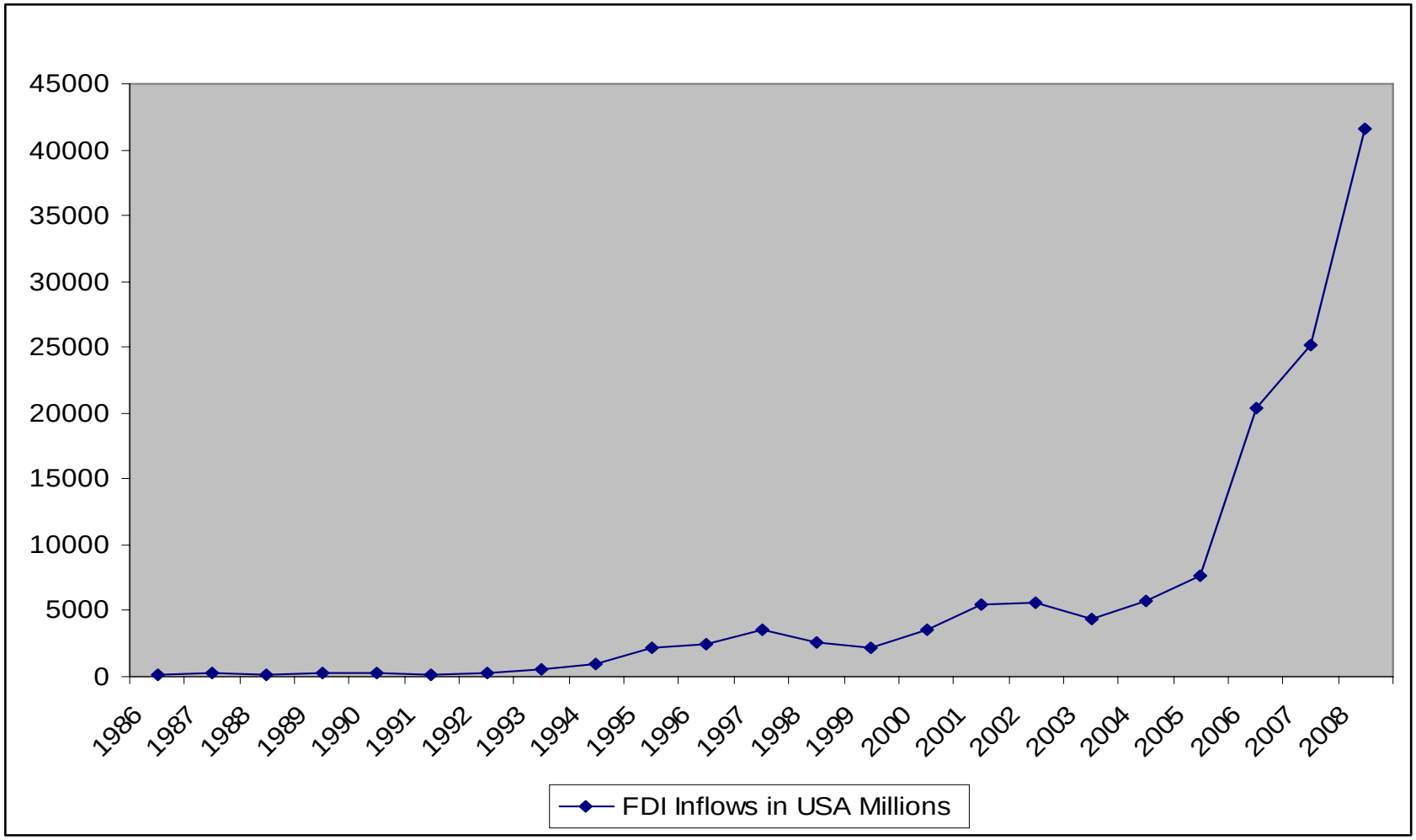
Impact of FDI Policy reforms

- Increase in FDI inflows
- Realisation of FDI inflows (Increase in actual flows as % of approval)
- Increase in FDI through automatic route
- More financial collaboration and increase in non-acquisition mode
- FDI from large number of countries

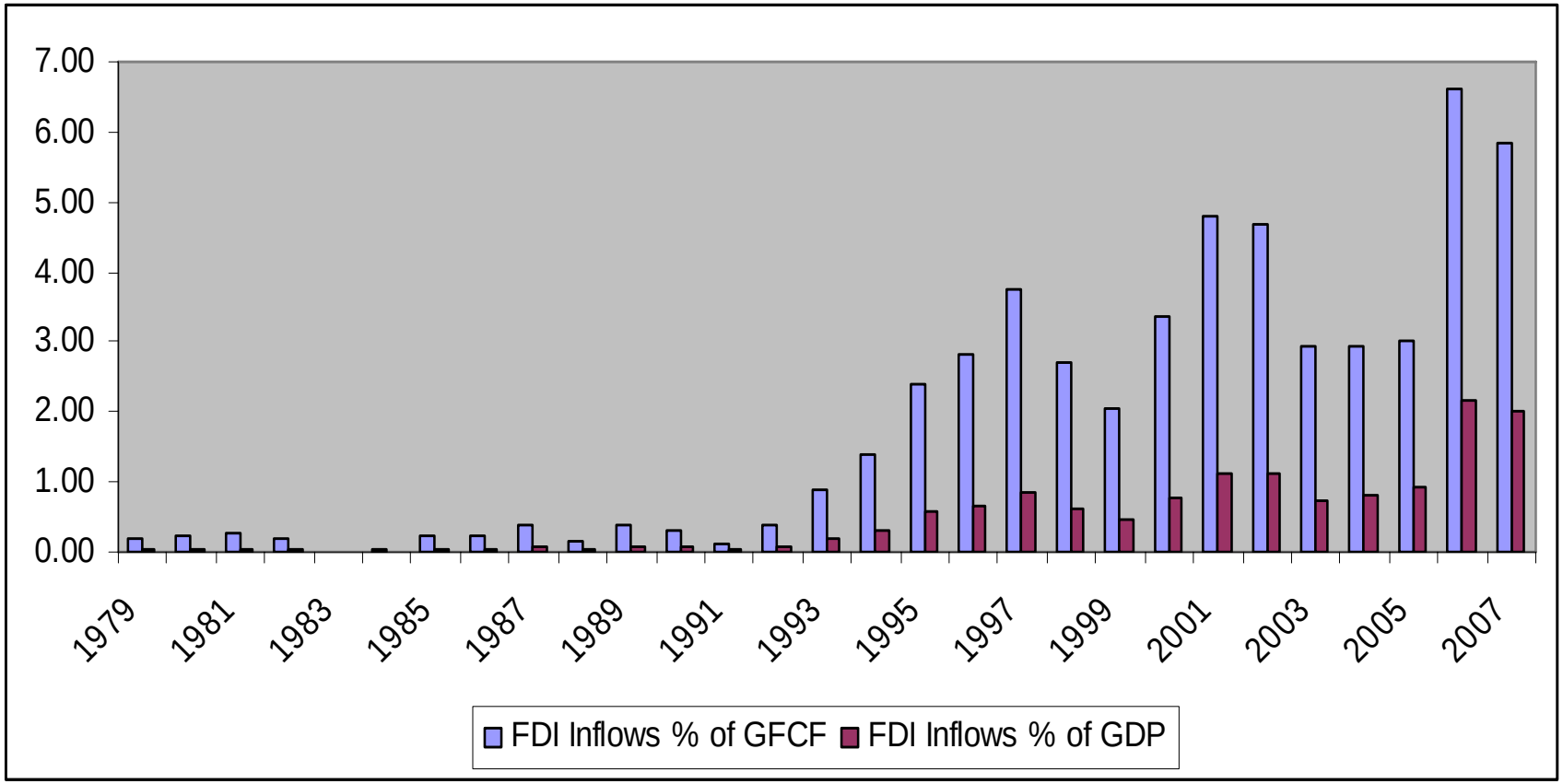
India: Trends in FDI Inflows

Indicators	1980	1985	1990	1995	2000	2005	2010
	Annual inflows						
Total FDI Inflows (million$)	**79.2**	**106**	**236.7**	**2151**	**3587**	**7621**	**24639**
% of GDP	**0.04**	**0.04**	**0.07**	**0.58**	**0.77**	**0.91**	**1.44**
% of GCF	**0.18**	**0.17**	**0.26**	**2.0**	**3.17**	**2.65**	**4.2**
Per Capita FDI (in $)	**0.11**	**0.14**	**0.27**	**2.25**	**3.40**	**6.7**	**20.2**
	FDI Stock						
Total FDI Stock (million$)	452	747	1656	5640	16338	43201	197939
% of GDP	0.25	0.33	0.50	1.52	3.50	5.2	11.5
% of GCF	1.6	1.24	1.8	5.2	14.5	15	33
Per Capita FDI (in $)	0.8	1.2	2.4	7.2	18.7	45	188
	Annual Outflows						
Total FDI Outflows (million$)	4	3	6	119	514	2985	14626
% of GDP	0	0	0	0.03	0.11	0.30	0.85
% of GCF	0	0	0.004	0.11	0.45	1.03	2.44
Per Capita FDI-Outflows (in $)	0	0	0.006	0.12	0.49	2.6	12

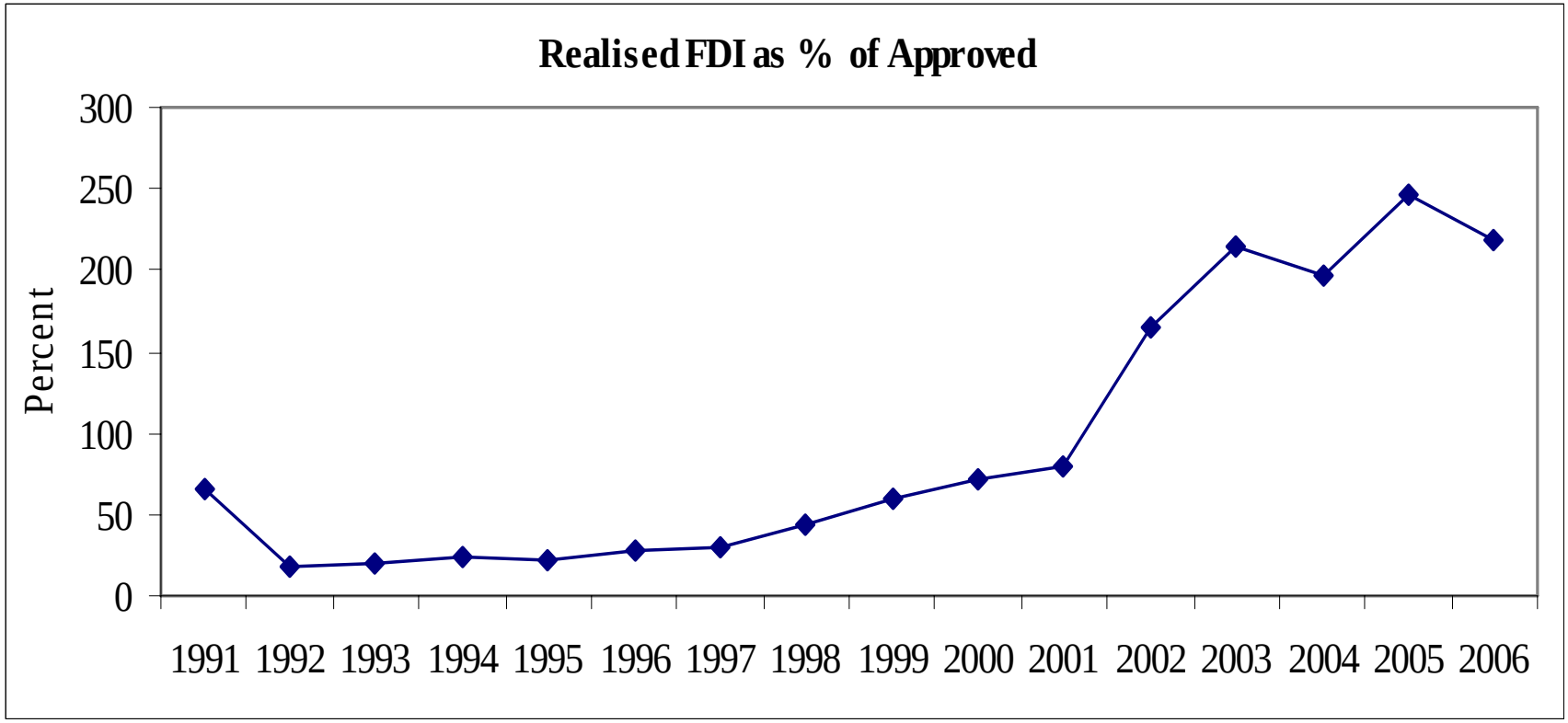
FDI Inflows into India: 1980 to 2008 (US Millions Dollar)



FDI as Percentage of GFCF and GDP



Actual FDI Inflows as Percentage of Approved FDI



India: Top Ten Sector-wise FDI (% Share in Total FDI)

	Aug. 1991-2005		2008-09	2009-10	2010-11	2000-2010
Electrical Equipments	14.13	Services Sector	22.6	16.2	17.0	21
Telecommunications	8.66	Telecommunications	9.3	9.8	8.6	8
Transportation Industry	8.17	Computer Software & hardware	5.7	3.4	4.0	8
Services Sector	7.94	Housing and real estate	10.4	11.4	6.3	8
Fuels (Power + Oil Refinery)	6.63	Construction activities	7.3	11.0	5.7	7
Chemicals	5.51	Automobile Industry	4.2	4.8	6.7	5
Food Processing Industries	3.03	power	3.3	4.9	6.5	4
Drugs & Pharmaceuticals	2.59	Metallurgical Industries	3.5	1.6	5.7	3
Cement and Gypsum Products	1.92	Petroleum and Natural gas	1.3	1.0	2.9	2
Metallurgical Industries	1.68	Chemicals	2.4	1.4	2.1	2

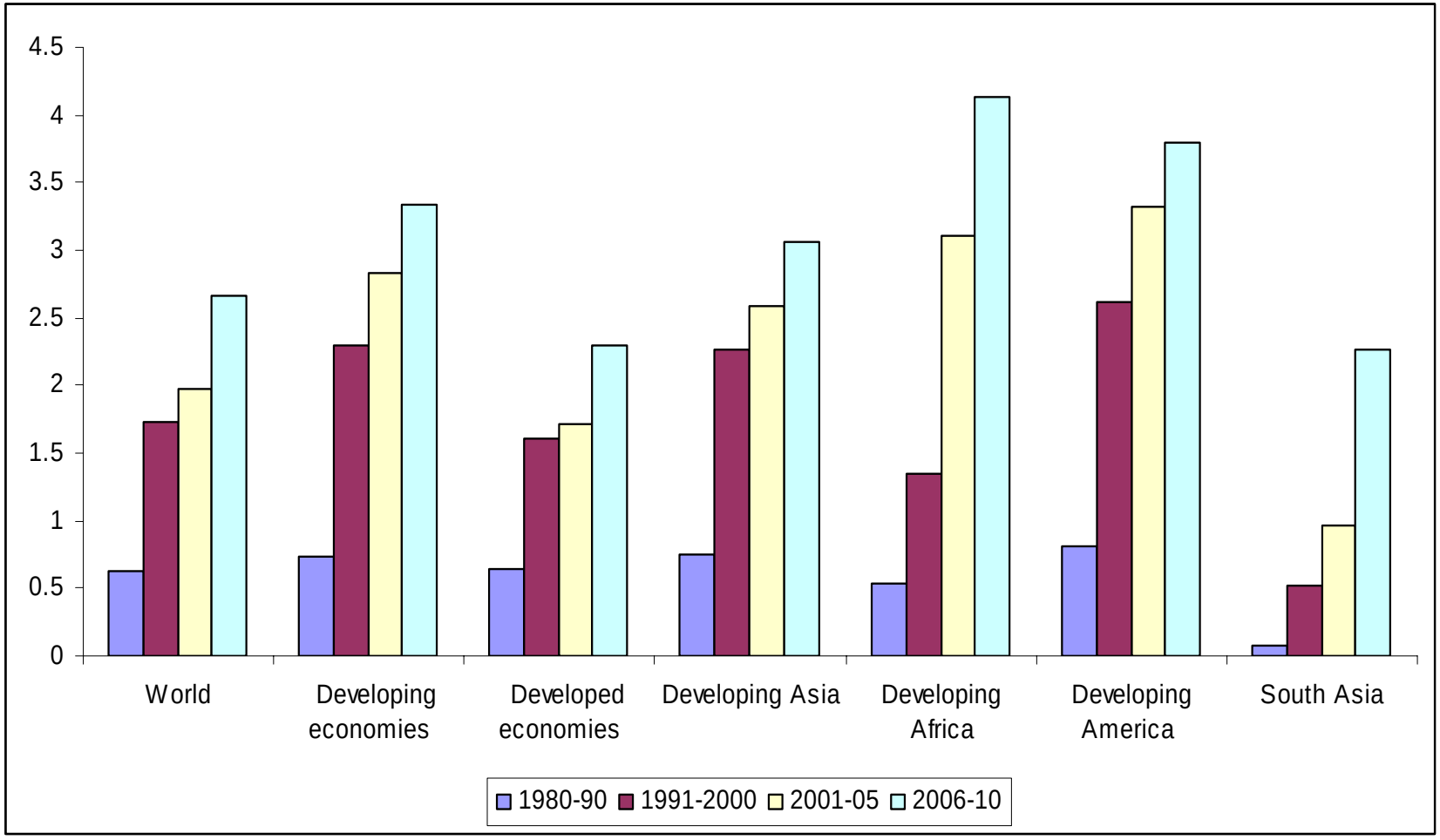
India: FDI Share of Top Countries (% share)

Countries	Aug. 1991-2000	2005-06	2008-09	2009-10	2010-11	2000-2010
Mauritius	10.6	46.3	41.1	40.2	36.0	42
Singapore	2.0	5.0	12.6	9.2	8.8	9
USA	21.9	9.1	6.6	7.5	6.0	7
UK	7.5	4.8	3.2	2.5	3.9	5
Ntherlands	2.2	1.4	3.2	3.5	6.2	4
Japan	4.3	3.8	1.5	4.6	8.0	4
Cyprus	0.0	1.3	4.7	6.3	4.7	4
Germany	3.8	5.5	2.3	2.4	1.0	2
France	2.4	0.3	1.7	1.2	3.8	2
UAE	0.3	0.9	0.9	2.4	1.8	1
Developed Countries	64	42	43	42	52	46
Developing Countries	36	58	57	58	48	54
Total	100	100	100	100	100	100

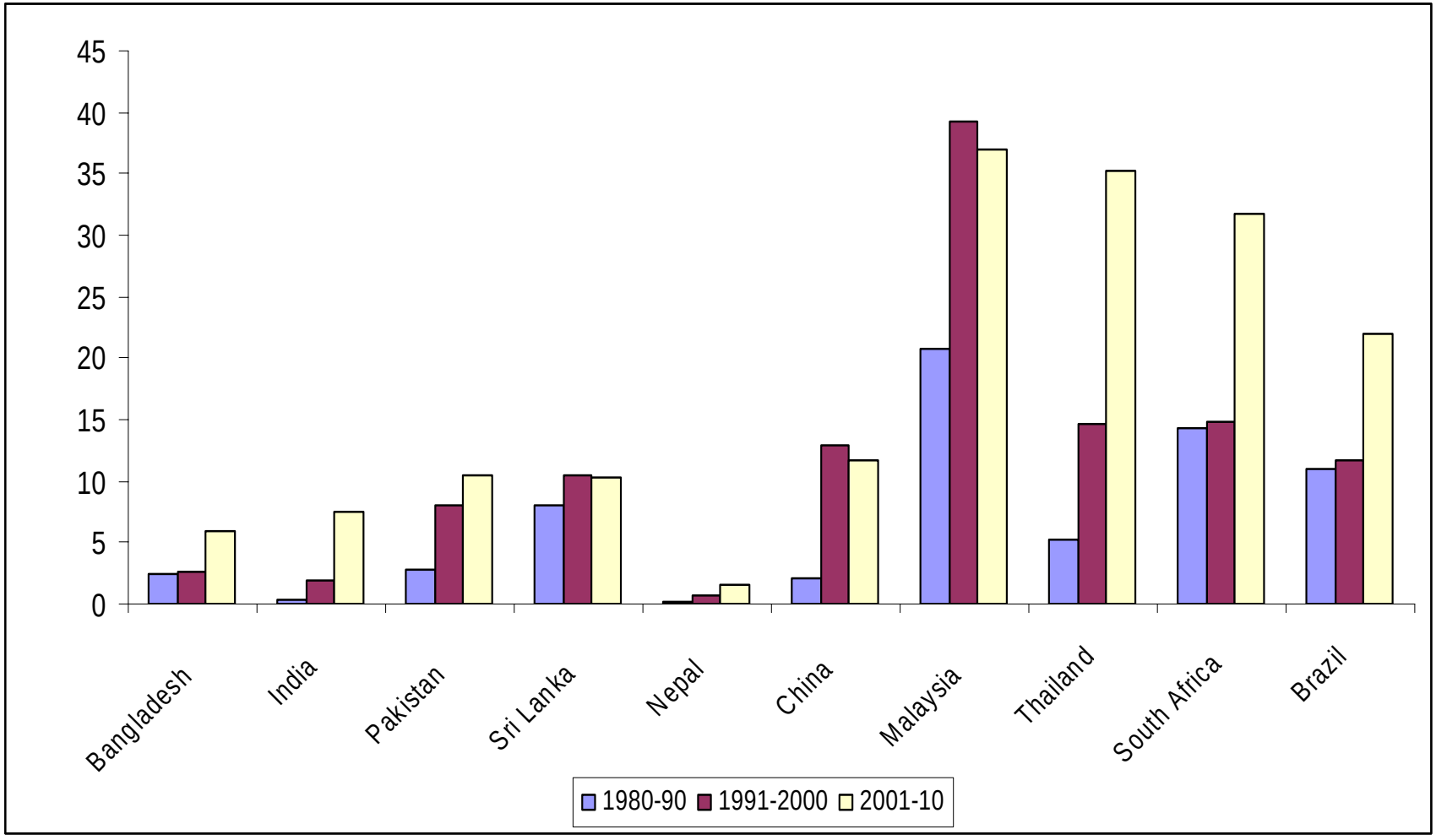
Political Economy of FDI Reforms in India

- Economic crisis-Need for non-debt creating sources of finances
- IMF conditionalities under CCFF
- Failure of Socialistic countries like USSR and East European and success of China
- Success of partial liberalisation in eighties
- Political background before reforms
- Emergence of Political Parties
- Competitive politics for market reforms and growth
- Balanace between beneficiaries and losers
- FDI allowed gradually in competing sectors

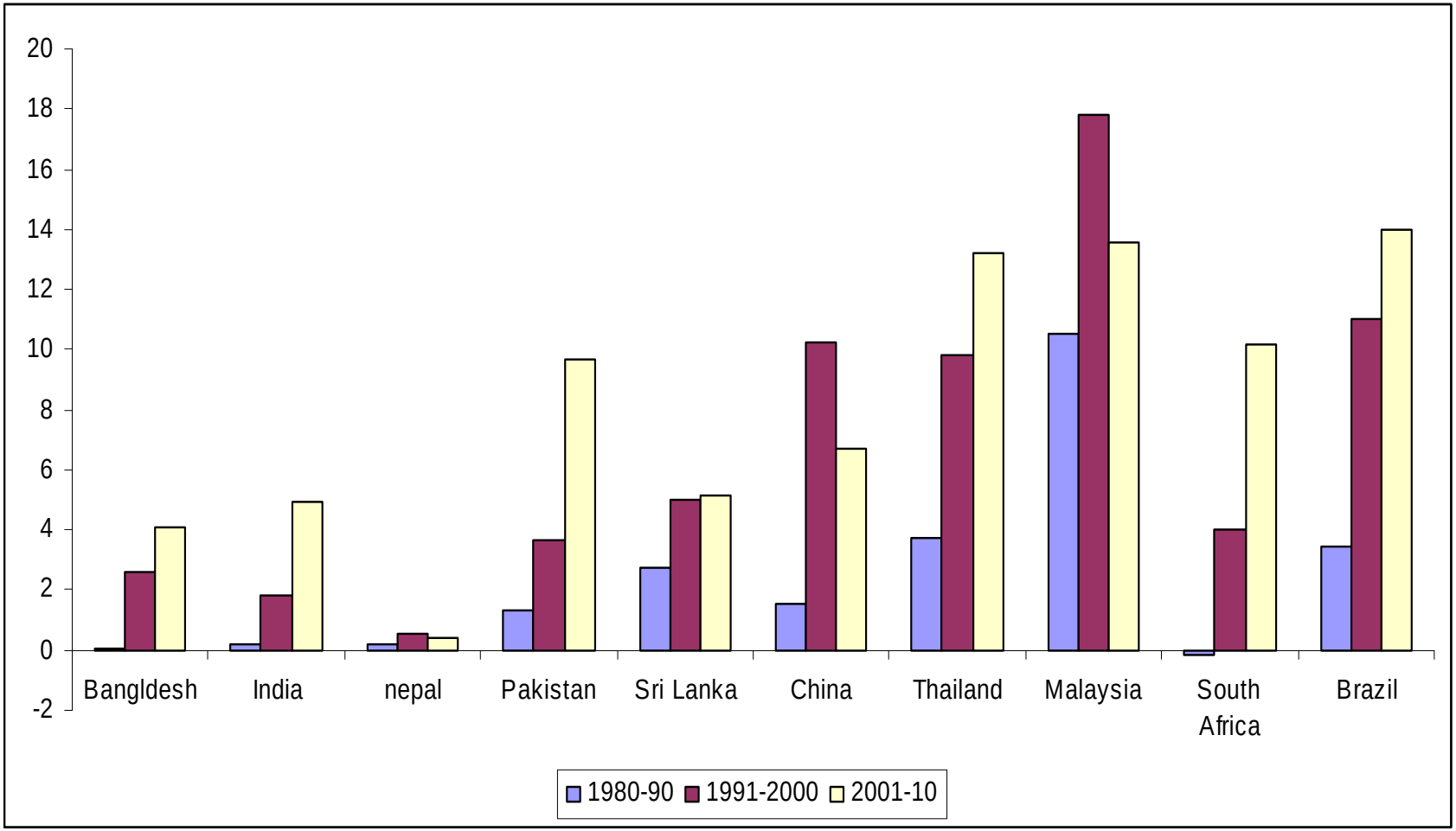
FDI inflows as ratio of GDP: Across Regions



FDI Stocks as ratio of GDP: Across Countries



FDI inflows as ratio of Gross Fixed capital Formation: Across Countries



Doing Business rank

	India	Bangladesh	Nepal	Pak	SLanka	China
Measures of Tax Burden						
Profit tax (%)	22.9	27.3	20.3	13.9	26.5	12
Labor tax and contributions (%)	18.2	0	11.3	12.6	16.9	58.9
Other taxes (%)	30.4	12.2	2.5	2.3	20.3	9
Total tax rate (% profit)	71.5	39.5	34.1	28.9	63.7	79.9
The costs imports and exports						
Cost to export (US$ per container)	**945**	**970**	**1,764**	**611**	**865**	**460**
Cost to import (US$ per container)	**960**	**1,375**	**1,900**	**680**	**895**	**545**
Difficulty of enforcing commercial contracts						
Procedures (number)	**46**	**41**	**39**	**47**	**40**	**34**
Duration (days)	**1,420**	**1,442**	**735**	**976**	**1,318**	**406**
Cost (% of claim)	**39.6**	**63.3**	**26.8**	**23.8**	**22.8**	**11.1**

Note: Doing Business WB.

Factor Affecting FDI inflows

- **Important Labour rules and regulations**
  - Rigid laws in case of lays off
  - Provision in contract labour
  - Trade union act

- **Under developed infrastructure**
  - Crucial for FDI, more so for export oriented FDI
  - Increase in supply-demand gap

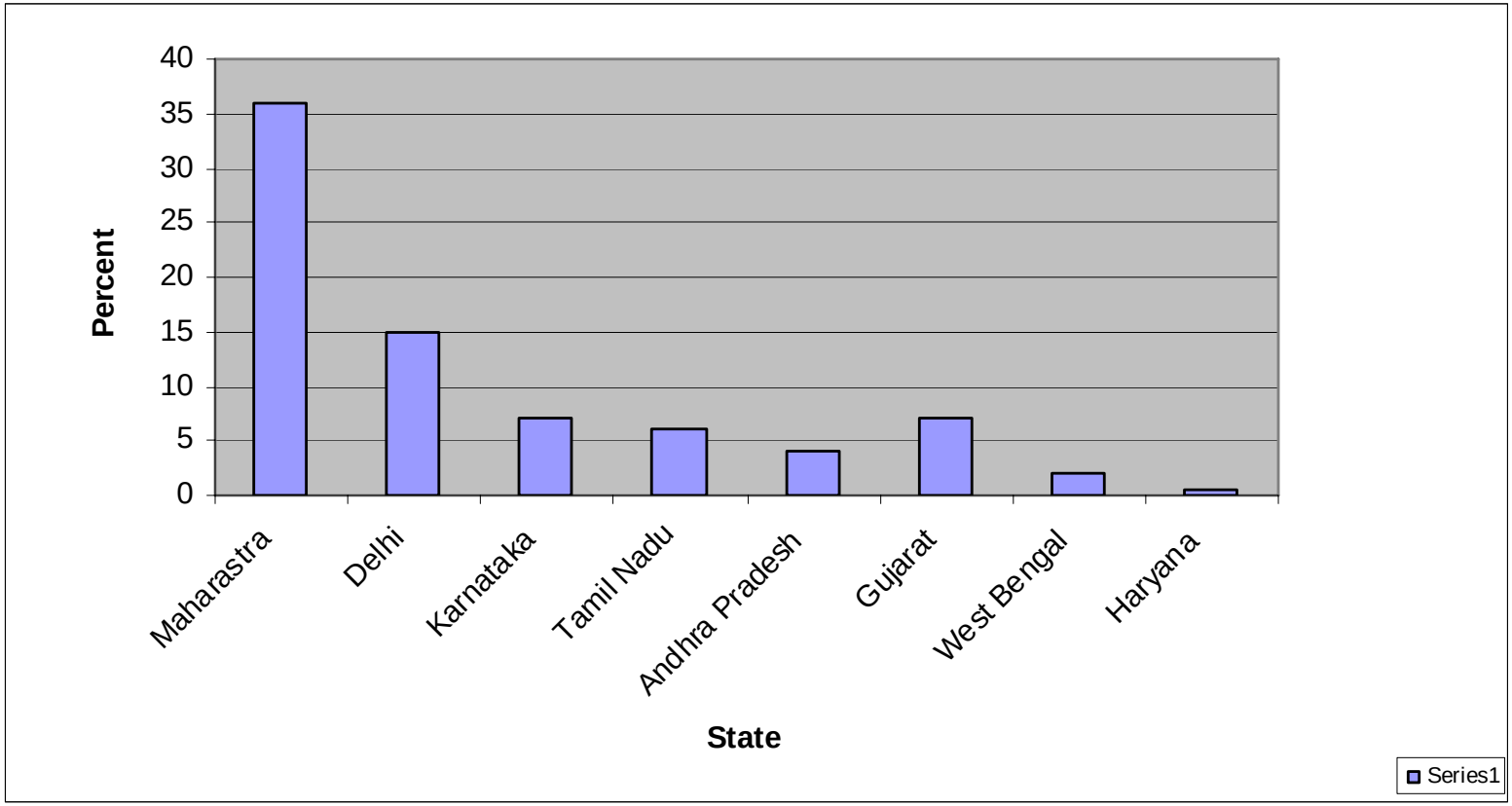
- **Major issues in Infrastructure sector**
  - Public-private partnership
  - Financing infrastructure
  - Fiscal measures, governance and incentives

- **Special Economic Zones**
  - Failure of EPZs
  - Incentives for SEZs
  - Major concerns of SEZs

- **Trade reforms and FDI**
  - FDI-Export-led Growth
  - Reduction of Tariffs and Non-tariff barriers, RTAs

Statement on RBI's Regional Office-wise Breakdown of FDI Inflows

(% share in total)



Source: "FDI Fact Sheet April 2000 to March 2009," Secretariat of Industrial Assistance

Note: Maharastra covers Dadra & Nagar Haveli, Daman & Diu
Delhi covers parts of UP and Haryana
Tamil Nadu Covers Pondicherry
West Bengal covers Sikkim, Andaman and Nicobar
Haryana covers Chandigarh, Punjab, Himachal Pradesh

State level reforms

- Five states receive 75% of total FDI inflows
- pro-market government
- Automatic bodies for single window clearance
- Incentives in SEZs, efforts to provide quality
- Infrastructure
- Pro-active and foresighted industrial policy

Difficulties for FDI: unfinished Agenda

- Infrastructure Bottleneck
- Rigid and complicated laws
- Lack of coordination between centre and States
- Ceilings and caps on foreign equity
- Time taking procedures

Steps to improve Investment climate and attract FDI

- **Infrastructure Development**
  - Independent regulatory mechanism
  - Dispute resolution mechanism
  - Cost-recovery based pricing
  - Increasing foreign equity to 100%
  - Special Investment law
  - Addressing issue relating to financing
- **Flexiable labour laws**
  - Setting up commission/committee to unify and harmonise labour laws
  - Addressing all rigid labour laws

- **Better coordination between centre and States**
  - Autonomous body to get clearances from both
  - State level reforms in coordination with centre
- **Making SEZs More Effective**
  - Proper designing and planning
  - Sufficient infrastructure connectivity
- **Further Institutional reforms**
  - Empowering FIPB for giving central level clearnces
  - Non-governmental facilitation centre
  - Trade reforms, privatisation of PSU

Latest FDI Policy Updates

- FDI in Multi Brand retailing
  - Policy Provisions
  - Expected Impact
  - Flip-flop in Policy and latest update
- Banking Amendment
- Insurance Bill
- Pension sector reforms
- Civil Aviation

Latest FDI Policy Updates

- Retrospective Tax reversal
- GAAR
- Goods and Services tax
- Direct tax code

Thank You