

## RSTV

### FDI Inflows - 13 JUNE, 2022

# FDI



#### What is FDI?

- Foreign direct investment (FDI) is a category of **cross-border investment** in which an investor resident in one economy establishes a lasting interest in and a significant degree of influence over an enterprise resident in another economy.
- FDI is a **key element in international economic integration** because it creates stable and long-lasting links between economies.
- FDI is an important channel for the **transfer of technology** between countries, promotes **international trade** through access to foreign markets, and can be an important vehicle for economic development.

#### Routes of FDI

- Today, the country is one of the most attractive destinations for foreign direct investments. Prime Minister Narendra Modi calls India a **land of 'golden opportunities.'**
- Foreign direct investment by an individual or a company based outside the country is regulated through two routes- the automatic route and the approval route.

##### The automatic route

- Under this route, investment into different sectors is **less restricted**. Foreign direct investment norms and regulations are more liberalized. Here, the overseas investor or the Indian company does not require prior approval from the Reserve Bank of India (RBI) or the government of India for investment in the country.

##### Approval route

- The approval route is a **little restricted**. The foreign investor or the Indian company has to take prior approval from the Reserve Bank of India (RBI) or the government of India before investing.

## Why in news?

- Recently, India has emerged as a **preferred investment destination** with FDI inflows increasing 20-fold in the last years.
- The **highest ever annual FDI inflow** of 83.57 billion US dollars was recorded in the Financial Year 2021-22.
- In **terms of investors** countries of FDI Equity inflow,
  - **Singapore is at the top with 27%**
  - followed by the U.S.A with 18% and
  - Mauritius at 16% for the FY 2021-22
- In **terms of sectors**, out of total FDI received,
  - **Computer Software & Hardware emerged as the top FDI recipient with 25%**
  - Service sector with 12%
  - Automobile Industry with 12%
- In **terms of State**, **Karnataka** has received the majority share of FDI equity in the 'Computer Software & Hardware' sector.
- In past years, to promote FDI in India, the government has adopted various **investor-friendly policies**, wherein most sectors except certain strategically important sectors are open for 100% FDI under the automatic routes.
- 853 FDI proposals have been disposed of through the **Foreign Investment Facilitation Portal** in five years since the abolishment of the Foreign Promotion Board (FIPB).

## What does the surge in FDI inflow indicate?

- The major **FDI inflows are coming** to sectors like Information Technology (IT) where the **return is expected to be maximum**.
- Even FDI tracking shows that the sectors in which investment is made are showing higher growth potential.
- For FY 2021-22, the Indian economy is expecting quite a few interesting deals to further increase FDI inflows.
- As compared to FY 2020-21, the FDI has not grown much.
  - **2020-21 was an exceptional year of pandemic**. Under which **large-scale investment** has been witnessed in India.

## Why there was a sharp increase in FDI during COVID-19 (FY 2020-21)

- In the **last eight years**, the government has adopted several measures with a focus on bringing up FDI inflows.
  - **Extended** sectoral caps in many sectors, like; Agriculture & Animal Husbandry and Plantation, etc.
  - Simultaneously, the government **expanded** the automatic routes under FDI inflows, like; Mining, Coal & Lignite and Broadcasting, etc.
  - **Diluting** several clauses by allowing single-brand retailers to start online sales.
- Various other initiatives to **boost manufacturing in India** have also increased FDI inflows in India:
  - Reduction in **corporate tax** from 30 per cent to 22 per cent.
  - Keeping in view India's vision of becoming 'Atmanirbhar' the government has also announced **production linked incentive (PLI) schemes** for 14 key sectors of manufacturing.
  - Promotion of electronics manufacturing has been a key component of the **Make in India program**.
  - Various state governments are also promoting manufacturing sectors.
- Investors around the world **ranked India as the 3<sup>rd</sup> most attractive destination for FDI**, 80% will invest in the next few years of which roughly \$500 billion has been invested already.
- Other than that Indian **Prime Minister's meeting with top CEOs** of the world with several Union Ministers following individually has attracted investment during FY 2020-21.

## Perspective from sector

- FY 2021-22 FDI inflows' highest share in Computer-IT was on expected lines.
- However, with a **\$193 billion deficit in trade**, India has been pitching for a **manufacturing hub**. The government is investing heavily in manufacturing as it is important to understand and facilitate the manufacturer.
- India's FDI inflows tend to increase or get strong in the next 4-5 years. **India is offering a combination of sectoral sides**, in the IT sector, India is offering a **skilled workforce**, whereas in the manufacturing sector India is offering a large **labour force**.
- India's **supply chain mechanism** is going to be a big driver.
- At the global level, the recent **Chinese spat with the U.S.A**, Australia and Germany have forced foreign investors to look for markets other than China. Vietnam tends to be too small to handle global demand, hence, **India is considered the best alternative to China**.

## Why upward movement in FDI in coming years?

- The upward movement is **based on three pillars**:
  - Huge consumer **demand** in India
  - **Government policy** to support FDI
  - India's strong **economic fundamentals**
- The upward movement is being tied with the **strategic effort** by India like diplomatic outreach by PM and various Union Ministers, economic alliance with other countries like **Free Trade Agreement (FTA)** will pay off and tie in the defence sector will further deepen.
- **EY Europe Attractiveness Survey 2022** indicates India will attract \$120-160 billion by 2025.
- With defence, the **space sector will also open up for FDI inflows**.
- PLI scheme in 14 sectors will allow the foreign-based company in India. Among them, IT and the digital sector will grow the most.
- In manufacturing, the **live portal** to help ease of business, **GATI Shakti on logistics** and investment in **infrastructure** will also pave upward movement in FDI.

## Most FDI comes from which country and what does this indicate?

- Mauritius was the leader in FDI inflows of India, but since India-Mauritius **Double Taxation Avoidance Agreement (DTAA)** is decreased significantly and will even decrease more in coming times.
- For FY 2021-22, **Singapore proved to be the top FDI investor for India**.
- As per the current trend, the major economic policies like **FTA are corresponding to FDI**. In other words, countries signing FTA are exchanging investments.
- Hence, many FDI is expected to come from countries with which India signed or will sign FTAs.

## What more needs to be done to maintain upward movement?

- The **Ease of Doing Business (EoDB)** has brought important improvement in investment in the past. Yet there is a **need to ensure more innovative ways to further improve EoDB** in India and at par with Singapore and U.S.A.
- Government must ensure '**what we are plan to invest get invested**'.
- More and more products and companies should be brought into **PLI-Scheme** and should be continuously **updated**.
- Need to increase the **confidence of investors** by ensuring fairness working in India and respecting international arbitration.
- Other than that, **direct tax reforms** in line with indirect tax reform to simplify like reform in Direct Tax Board (DTB) and other comprehensive reforms in line with the needs of the \$5 trillion economies.

There are various reasons behind India becoming a preferred destination for investors across the world in terms of FDI inflows hitting a record high in FY 2021-22. But there is still a lot more to be done with evolving policies and also making it more lucrative to come and invest in India.



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