Advances in Economics and Business Management (AEBM)
p-ISSN: 2394-1545; e-ISSN: 2394-1553; Volume 4, Issue 2; January-March, 2017, pp. 126-135

http://www.krishisanskriti.org/Publication.html

Role of FDI in Economic Development of India-Issues, Opportunities and Challenges

Swami Prakash Srivastava[1] and Sachin Prakash Srivastava[2]

[1]*Dept. of Economics & Dean, Faculty of Social Science, Dayalbagh Deemed University-Agra-282005*
[2]*Students of MBA-Final Year, RBS Management and Technical Campus-Agra*

Abstract—*FDI is considered to be the life blood and an important vehicle for economic development as far as the developing nations are concerned. The important effect of FDI is its contribution to the growth of the economy. According to a recent survey by the United Nations Conference on Trade and Development (UNCTAD), India has conspicuously emerged out as the second most popular and preferable destination in the entire world, after China, for highly profitable foreign direct investment. The sectors which attracted higher inflows were services,. Telecommunication, construction activities and computer software and hardware. Mauritius, Singapore, the US and the UK were among the leading sources of FDI. The global survey of leading consultancy firm EY has ranked India as the most attractive investment destination followed by Brazil and China at second and third positions, respectively. With sharp currency depreciation and opening up of FDI in various sectors, India has become an attractive destination for foreign investors.*

India's perception abroad has been changing steadily over the years. This is reflected in the ever growing list of countries that are showing interest to invest in India. FDI in the country has touched an all time high of USD 40 billion in 2015-16. Foreign investment is crucial for India, which needs about $1 trillion by March 2017 to overhaul infrastructure such as ports, airports and highways, and to boost growth. Other nations from where foreign inflows are increasing include Japan , the Netherlands, the US, Germany, France and the UAE during the last financial year.

Apart from being a critical driver of economic growth, foreign direct investment (FDI) is a major source of non-debt financial resource for the economic development of India. Foreign companies invest in India to take advantage of relatively lower wages, special investment privileges such as tax exemptions, etc. For a country where foreign investments are being made, it also means achieving technical know-how and generating employment. The Indian government's favourable policy regime and robust business environment have ensured that foreign capital keeps flowing into the country.

Keywords*: Foreign Portfolio Investment, NRI, FIPB, DTAA, Technology transfer, GAAR.*

1. INTRODUCTION

The fast and steadily growing economy of India in majority of its sectors, has made India one of the most famous and popular destinations in the whole world, for Foreign Direct Investment. India's ever-expanding markets, liberalization of trade policies, development in technology and telecommunication, and loosening of diverse **foreign investment restrictions**, have further collectively made India, the apple of investors' eye, for most productive, profitable, and secure foreign investment.

India's perception abroad has been changing steadily over the years. This is reflected in the ever growing list of countries that are showing interest to invest in India. Mauritius emerged as the most dominant source of FDI contributing 44 % of the total investment in the country. Singapore was the second dominant source of FDI inflows with 9% of the total inflows. However, USA slipped to third position by contributing 7% of the total inflows. UK occupied fourth position with 5% followed by Netherlands with 4%, Japan with 4%, Cyprus with 4%, Germany with 3%, France with 1%, UAE with 1%.

Section II

Review of Literature

K S Chalapathi Rao, Professor, ISID-NewDelhi-2016: Most of the FDI coming into India through Mauritius, Singapore and Cyprus are actually from the U.S. or from India-related investors. The Mauritius route is used for availing tax benefits and for ensuring anonymity. FDI from Mauritius is however sector-agnostic unlike FDI from countries like Japan, Germany and France, which are mostly in manufacturing-related sectors. The Singapore route is used mostly by Indian entities with a regional office there.

Dhiraj Mathur, partner, PwC: Several companies including from India had taken advantage of the concessions given by the Singapore government to set up regional headquarters there. These companies had also raised money in Singapore to in turn invest in India and other countries,

United Nations Conference on Trade and Development (UNCTAD) World Investment Report 2015 : India acquired ninth slot in the top 10 countries attracting highest FDI in 2014. FDI inflows to India are likely to exhibit an upward trend on account of economic recovery. India also jumped 16 notches to 55 among 140 countries in the World Economic Forum's Global Competitiveness Index that ranks countries on the basis of parameters such as institutions, macroeconomic environment, education, market size and infrastructure among others.

Jose Manuel Durao Barroso, President, European Commission (2013) : Europe is India's largest source of foreign direct investment with a stock of 34.4 billion euros and India's investments in Europe is also fast reaching 7 billion euros. There is scope to grow much more. European FDI in India for instance is half the amount of that in China, or a quarter of that in Russia, or a fifth of that in Brazil,"

E & Y Survey(2014): The global survey of E& Y has ranked India as the most attractive investment destination followed by Brazil and China at second and third positions, respectively.

Section III

Significance of FDI in India

Foreign direct investment (FDI) in India has played a very important role in developing the Indian economy. FDI in India has – in many ways – enabled India to achieve a certain degree of financial growth, stability and financial development. It has allowed India to focus on areas that needed economic attention, and address various issues that continue to challenge the country. FDI in India has increased over a period of time due to the efforts been made by the Indian government. The increased flow of FDI in India has given major boost to the country's economy and hence steps should be taken to make sure that the flow of FDI in India continues to grow. FDI investments are permitted through private equity or preferential allotments, financial collaborations, through capital markets in form of Euro issues, and in joint ventures.

FDI has an important impact on country's trade balance, increasing labour standards, transfer of technology and innovative ideas, skills and the general business climate. FDI also provides opportunity for technological transfer and up gradation, access to global managerial skills and practices, optimal utilization of human capabilities and natural resources, making industry internationally competiteve, opening up export markets, aceess to international quality goods and services and augmenting employment opportunities.

Section IV

Present status of FDI inflow in India

India's share in global FDI has increased considerably, but the pace. of FDI inflows has been slower than China, Singapore, Brazil, and Russia. Indian economy is largely agriculture based and here is plenty of scope in food processing, agriculture services and agriculture machinery. FDI in this sector Research and Development expenditure shows unexpected should be encouraged. negative sign. This could be attributed to the fact that R&D sector is not receiving enough FDI as per its requirement. but this sector is gaining more attention in recent years.

Background

In 1991, still tainted in the world's eyes by its failed experiment with socialism, India attracted a meager $240 million in inflows, less than a fourth of what Indonesia managed. Last year, more than $44 billion worth of FDI poured into India, about three times what Indonesia attracted , and a staggering 183 times more than the 1991 figure. The IMF estimates that Indian per capita income more than tripled from about $550 in 1991 to $1,800 last year. As a result, an entire generation has grown up expecting upward mobility, where their parents and grand parents accepted stagnation. At the same time, India's weight in the world has grown. In 1991, , the worlds second most populous country accounted for a scant 3.6% of global gross domestic product. By 2015, this had nearly doubled to 7%. The world Bank estimates that India's trade to GDP ratio nearly tripled from 16.7% in 1991 to 49% in 2014. Simply put, pre reform India was economically insignificant and cut off from the world. Today, it is an important player in the global economy. And as dependent on trade for its prosperity as China or Indonesia.

FDI inflows in FY 16

Foreign direct investment (FDI) inflows into India in 2016 calendar year jumped 18% to a record $46.4 billion, at a time global FDI inflows fell. Data released by the Department of Industrial Policy and Promotion (DIPP) showed FDI inflows in 2016 were strongest in October with $6.2 billion inflows followed by $5.1 billion in September. Global flows of FDI fell 13% in 2016 to an estimated $1.52 trillion as global economic growth remained weak and world trade volumes posted anemic gains, according to the latest UNCTAD Global Investment Trends Monitor. FDI recovery continues along a bumpy road. Particularly of concern is the sharp drop-off in manufacturing investment projects, which play such an important role in generating badly needed productivity improvements in developing economies. UNCTAD said FDI inflows into India fell 5% to $42 billion in 2016, yet India stood as the 10th most attractive destination in the world for FDIs. In comparison, China and Brazil received $139 billion and $50 billion FDI inflows respectively during 2016. The US remained the top source of FDI inflows in 2016 at $385 billion. Mauritius remained India's top source of FDI inflows at $12.8 billion followed by Singapore at $7.1 billion during April-December period. Services sector continued to attract highest investment of $7.5 billion followed by telecommunications sector which attracted $5.5 billion inflows during the first nine months of the financial year 2016-17.

Road ahead

According to United Nations Conference on Trade and Development (UNCTAD) World Investment Report 2015, India acquired ninth slot in the top 10 countries attracting highest FDI in 2014 as compared to 15th position last year. The report also mentioned that the FDI inflows to India are likely to exhibit an upward trend on account of economic recovery. India also jumped 16 notches to 55 among 140 countries in the World Economic Forum's Global Competitiveness Index that ranks countries on the basis of parameters such as institutions, macroeconomic environment, education, market size and infrastructure among others. India will require around US$ 1 trillion in the 12th Five-Year Plan (2012–17), to fund infrastructure growth covering sectors such as highways, ports and airways. This would require support from FDI flows. During 2014, foreign investment was witnessed in sectors such as services, telecommunications, computer software and hardware, construction development, power, trading, and automobile, among others.

Outward FDI

After witnessing a sharp increase during FY 07-11, outward FDI had been declining in the subsequent period. This has been largely due to the impact of the global financial crisis of 2008 and a strong rupee which was associated with such outflows. These outflows have tended to concentrate in sectors such as transport, storage, communications, and manufacturing and also in geographies like the Netherlands , Singapore, Mauritius, British Virgin Islands, USA, the UK and UAE.

State-wise Analysis of FDI Inflows

A state-wise analysis of FDI inflows by the economic survey shows that Delhi, Haryana, Maharashtra, Karnataka, Tamil Nadu, Gujarat and Andhra Pradesh together attracted more than 70% of total FDI inflows to India during the last 15 years. States with vast natural resources like Jharkhand, Bihar, Madhya Pradesh, Chhattisgarh and Odisha have lagged behind. To make the recently launched Make in India initiative a success, the states will have a critical role in facilitating FDI in different sectors.

Since investments until March 31, 2017 have been exempted from capital gains tax, there is no risk of an immediate outflow of funds. However, the protocol will impact all prospective investments with effect from April 1, 2017. Also, the benefit of the two-year transition period will be limited to companies that are not regarded as a shell/conduit company, and their total expenditure on operations in Mauritius has been at least Rs 27 lakh in the preceding 12 months. Experts feel that while some investors who are bullish on India may advance their plans and invest before April 1, 2017 in order to save tax, many others will raise their due diligence procedure on investments, factoring in the tax cost in the returns they generate.

Table 1.0

Break-Up of FDI Investment By India	
Guarantee Issued	65.1
Equity	23.9
Loans	11.0

Above table 1.0 shows the break up of FDI investment by India. The share of Guarantee issue is 65.1% , Equity 23.9% and loans 11.0 %. in the total FDI investment by India.

Section V

FDI in major sectors in India - Preferred Sectors:-

Major sectors of the Indian economy which have benefited from FDI in India are -Financial sector (Banking and Non-Banking), Insurance, Telecommunication, Hospitality and tourism, Pharmaceuticals, and Software and Information Technology etc. As shown in table 2.0 below. FDI is not permitted in the arms, nuclear, railway, coal or mining industries.

Table 2.0

Sect oral Distribution of FDI By India	
Sectors	**Distribution of FDI By India**
Transport, Storage and Communication Services	30.40
Manufacturing	25.81
Agriculture and Mining	16.50
Wholesale, retail trade, restaurants and hotels	9.91
Financial, Insurance and business services	8.02
Construction	4.80
Community, social and personal services	4.33
Others	0.30

Currently, FDI is allowed in financial services, including the growing credit card business. These also include the non-banking financial services sector. Foreign investors can buy up to 40% of the equity in private banks, although there is condition that these banks must be multilateral financial organizations. Up to 45% of the shares of companies in the global mobile personal communication by satellite services (GMPCSS) sector can also be purchased. A number of projects have been implemented in areas such as electricity generation, distribution and transmission, as well as the development of roads and highways, with opportunities for foreign investors. The Indian national government also granted permission for FDIs to provide up to 100% of the financing required for the construction of bridges and tunnels, but with a limit on foreign equity of INR 1,500 crores, approximately $352.5 million.

Section VI

Impact of liberalization on FDI in India

FDI reforms in India

Rated among the top emerging nations, India's liberalization policies are paying rich dividends to the economy as a whole. India, post liberalization, has not only opened it's doors to foreign investors but also made investing easier for them by implementing the following measures:

A. FDI in the Retail sector:

Retailing is one of the worlds largest private industry. Liberalizations in FDI have caused a massive restructuring in retail industry. The benefit of FDI in retail industry superimposes its cost factors. Opening the retail industry to FDI will bring forth benefits in terms of advance employment, organized retail stores, availability of quality products at a better and cheaper price. It enables a countrys product or service to enter into the global market.

In Nov 2015 , the centre eased the rules permitting 100% FDI in ‘Single Brand Product Retail Trading’ subject to the sourcing caveat-the pre condition being that companies with more than 51% foreign ownership must source 30% of the value of goods in India, preferably from medium, small or micro enterprises. In isolation, the requirement of certain proportion of domestic content in the products has a socio-economic relevance, given its potential to create jobs and protect livelihoods. But the sourcing norm has inhibited FDI inflow ; worse, it could fall foul of the WTO’s National Treatment Norms. The centre, therefore, amended the condition allowing for an exemption to entities selling “products having ‘state of the art’ and ‘cutting –edge’ technology”, and even more ambiguously, in cases “where local sourcing is not possible”. Predictably Apple has sought waivers citing the exemption clause.

Cheaper production facilities:

FDI will ensure better operations in production cycle and distribution. Due to economies of operation, production facilities will be available at a cheaper rate thereby resulting in availability of variety products to the ultimate consumers at a reasonable and lesser price.

Availability of new technology:

FDI enables transfer of skills and technology from overseas and develops the infrastructure of the domestic country. Greater managerial talent inflow from other countries is made possible. Domestic consumers will benefit getting great variety and quality products at all price points.

Long term cash liquidity:

FDI will provide necessary capital for setting up organized retail chain stores. It is a long term investment because unlike equity capital, the physical capital invested in the domestic company is not easily liquidated.

B. Make in India Initiation and FDI in Manufacturing Sector

Foreign direct investment (FDI) in India has received a dramatic boost from the launch of the Make in India initiative, according to the latest Economic Survey. After the September 2014 launch of the initiative, which seeks to promote manufacturing and attract foreign investment, there was an almost 40% increase in FDI inflows from October 2014 to June 2015 over the year-ago period. Under the programme, the government has awarded 56 defence manufacturing permits to private sector entities in the past one year, after allowing 49% FDI in the defence sector in August 2014, compared with 47 granted in the preceding three years. Entities from several countries such as Japan, China, France and South Korea announced their intention to invest in India in various industrial and infrastructure projects. The concept of Make in India has really succeeded as it added more employment. With this, India has now become a vibrant market for manufacturers. For the products that are made out of the initiative, we have a strong domestic market with increasing demand. Infrastructure sector is where foreign investments can come in a big way. The major objectives behind the Make in India initiative are job creation and skill enhancement in 25 sectors of the economy, including automobiles, aviation, biotechnology, chemicals, construction, defence manufacturing, electrical machinery, electronic systems and mining.

C. FDI in Services Sectors

Services, telecommunications, construction, computers (software and hardware), real estate and housing, chemicals, drugs and pharmaceuticals, power, automobiles and metallurgical industries received the highest FDI inflows across India. Assocham has also called for a time-bound, non-discretionary, simplified and less number of procedures and approvals to help uplift overseas investors' confidence and foster more investments in India. In terms of sectors, services attracted the maximum investment this fiscal as per Department of Industrial Policy and Promotion (DIPP) data. However, in terms of growth, it was drugs and pharmaceuticals that saw the maximum jump, with an over 15-fold increase. In contrast, the automobile and housing and real estate sectors saw FDI decline. Investment in the petroleum sector jumped significantly too. Service sector has been the most sought after sector in India for Foreign Direct Investments.• India, with its skilled labor and manpower has the potential to overtake China as the most preferred destination for Foreign Investments. Hence measures must be taken in order to ensure that the flow of FDI in our country continues to grow.

Section VII

Role of Different Countries in FDI for India

Europe

Europe is India's largest source of foreign direct investment with a stock of 34.4 billion euros and India's investments in Europe is also fast reaching 7 billion euros. There is scope to grow much more. European FDI in India for instance is half the amount of that in China, or a quarter of that in Russia, or a fifth of that in Brazil. foreign direct investment with a stock of 34.4 bThe European Union is India's first partner in terms of trade and investment - in 2010 the European Union imported over 40 billion Euros worth of goods and services from India. Europe is also one of India's major partners in the field of economic and development cooperation, particularly in the areas of education and social actions. India has one of the highest potentials for the effective use of renewable energy and it is already the fifth largest producer of wind power; Europe has a large know-how in the green economy and we are developing a low-carbon economic strategy.

Mauritius and Singapore

Singapore, Mauritius, the Netherlands and the US account for the major share of FDI inflows into India. Out of FDI equity inflows of $24.8 billion during 2015-16 (April-November), more than 60% came from two geographically small countries—Singapore and Mauritius. These inflows need perhaps to be examined more closely to determine whether they constitute actual investment or are diversions from other sources to avail of tax benefits under the Double Tax Avoidance Agreement that these countries have with India..

Mauritius has regained the position as top source of foreign direct investment (FDI) into India by pushing Singapore to the second slot in 2014-15. Mauritius accounted for about 29 per cent of the country's total FDI inflows last fiscal. In 2013-14, Singapore had replaced Mauritius as the top source of FDI into India. According to the Department of Industrial Policy and Promotion, FDI inflows under the approval route (which requires prior government permission) increased by 87% during 2014-15 with an inflow of $2.22 billion. More than 90% of FDI was through the automatic route. Also in 2014-15, foreign institutional investment rose by an unprecedented 717% to $40.92 billion.

China

On top of this, there is around 60 billion dollors of remittance Indian send back to India annually. Which is highest in the world, even more then Chinese. This also shows Indian consider India as their long term save investment zone. This is important to note that more Indians see India as a safe destination for their investment as compare to Chinese considering investing back into China. Infact more and more millineries in China are taking out their wealth from China which is actually more then the total FDI china is getting now. The Chinese government have restricted the currency too much, there's nothing left for Chinese to buy in China and returns are very low that's why they're trying to get it out. But the government has serious restrictions in place and this remains a problem. They should float the RMB properly. India isn't perfect but it's international money flows are better than China's.

USA and other Countries

U.S. was the worlds largest recipient of FDI from OECD (Organization for Economic Co-operation and Development) countries. France, Greece, Iceland, Poland, Slovak Republic, Switzerland and Turkey also have a positive record in FDI investments.

Section VIII

Govt. initiatives

The Indian government's favourable policy regime and robust business environment have ensured that foreign capital keeps flowing into the country. The government 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. The state also competing among themselves to improve the ease of doing business by cutting down red tapism, bureaucratic and procedural hurdles. The FDI regime too has been liberalized substantially in the last couple of years. Some necessary legislations on insurance and pension reforms that opened up FDI further to up to 49 percent have been passed. These legislations were pending for several years. That apart, FDI in defence has been liberalized considerably attracting large commitments by foreign companies with Indian partners for hi tech defence productions.

Government Initiative- Budget 2016-17

Budget 2016-17 has proposed several reforms in Foreign Direct Investment (FDI) Policy in areas of insurance and pensions, asset reconstruction companies and stock exchanges, such as easier governing and fund raising norms, clarification of tax related matters and higher FDI limits.

1. Residency Permit Policy

In order to make India a more attractive foreign investment destination, the Ministry of Finance is planning to introduce the residency permit policy, which will allow key executives of foreign companies making investments worth US$ 2 billion or more in India, to avail various facilities such as special package on upscale housing, residency permits allowing long stay in the country, and cheap rates for utilities.

2. Construction Development Sector

The Government of India has amended the FDI policy regarding Construction Development Sector. The amended policy includes easing of area restriction norms, reduction of minimum capitalisation and easy exit from project. Further, in order to provide boost to low cost affordable housing, it has indicated that conditions of area restriction and minimum capitalisation will not apply to cases committing 30 per cent of the project cost towards affordable housing.

3. Relaxed foreign direct investment (FDI) policy in 15 sectors

The Government of India has recently relaxed foreign direct investment (FDI) policy in 15 sectors, such as raising the foreign investment limit for some sectors, easing the conditions for others and putting many on the automatic route for approval. The sectors that benefited from the relaxation include defence, real estate, private banking, defence, civil aviation, single brand retail and news broadcasting. The new rules provide for easier exit from investment in the construction sector while foreign investment limit in defence and airlines was allowed up to 49 per cent through the automatic route. Banks were allowed fungible FDI investment up to 74 per cent, which means that FII investment in private banks can rise to this limit. The Government of India recently relaxed the FDI policy norms for Non-Resident Indians (NRIs). Under this, the non-reparable investments made by the Persons of Indian Origin (PIOs), Overseas Citizens of India (OCI) and NRIs will be treated as domestic investments and will not be subject to FDI caps.

4. Insurence

The government has also raised FDI cap in insurance from 26 per cent to 49 per cent through a notification issued by the DIPP. The limit is composite in nature as it includes foreign investment in the form of foreign portfolio investment, foreign institutional investment, qualified foreign investment, foreign venture capital investment, and non-resident investment.

The Cabinet Committee on Economic Affairs (CCEA) has raised the threshold for foreign direct investment requiring its approval to Rs 3,000 crore (US$ 440.15 million) from the present Rs 1,200 crore (US$ 176.06 million). This decision is expected to expedite the approval process and result in increased foreign investment inflow. India’s cabinet cleared a proposal which allows 100 per cent FDI in railway infrastructure, excluding operations. Though the initiative does not allow foreign firms to operate trains, it allows them to invest in areas such as creating the network and supplying trains for bullet trains etc.

5. Most Favoured Nation (MFN) Treatment to 15 countries

India is likely to grant most favoured nation (MFN) treatment to 15 countries that are in talks regarding an agreement on the Regional Comprehensive Economic Partnership (RCEP),which would result in significant easing of investment rules for these countries. The Government of India plans to further simplify rules for Foreign Direct Investment (FDI) such as increasing FDI investment limits in sectors and include more sectors in the automatic approval route, to attract more investments in the country.

6. FDI in defence production

FDI in defence production is now allowed up to 49 percent through FIPB route.. In some hi-tech defence production it could up to 100 percent on case by case basis. More recently thee budget opened up multi brand retail on food items up to 100 percent FDI. Usually 70 percent of multi brand retail business would over is on food items. This will go a long way in improving the lot of rural India and farmers as exploitation by middle men will get phased out..

7. Abolition of FIPB; Finance Minister in his budget 2017-18 announced abolishing FIPB saying 90%of the foreign investment approvals are via automatic route and only 10% go to the board. Currently ,FIPB offers single window clearance for applications on FDI in India that are under the approval route. The sectors under automatic route do not require any prior approvals and are subject to only sectoral law.

Section IX

General Anti Avoidance Rules

In view of wide-spread concerns by foreign investors, the government had earlier postponed implementation of GAAR, which was introduced by the then finance minister Pranab Mukherjee in his Budget for 2012-13 to check tax evasion. The expert committee on General Anti Avoidance Rules (GAAR) recommended postponement of the controversial tax provision by three years and abolition of capital gains tax on transfer of securities. As a step towards reassuring global investors, the committee in its draft report, suggested that GAAR provisions should not be invoked to examine the genuineness of the residency of entities in Mauritius. Mauritius is the most preferred route for foreign investments because of the liberal taxation regime in the island country. India has a double taxation avoidance treaty with Mauritius.

The Shome committee

The committee, headed by Parthasarathi Shome, has recommended that GARR be applicable only if the monetary threshold of tax benefit is Rs 3 crore and more. The Shome committee was set up by Prime Minister Manmohan Singh to address the concerns of foreign investors. The draft report of the Shome committee said: "... GAAR should be deferred for 3 years. But the year, 2016-17, should be announced now. In effect, therefore, GAAR would apply from assessment year 2017-18. Pre-announcement is a common practice internationally, in today's global environment of freely flowing capital.

Impact of General Anti Avoidance Rules

India attracted USD 9.03 billion in FDI from Mauritius in 2014-15, whereas it was USD 6.74 billion from Singapore, according to the data of the Department of Industrial Policy and Promotion (DIPP). The benefits under tax treaty and deferment of General Anti-Avoidance Act (GAAR) by two years has helped investors. FDI inflows from Mauritius had declined due to fears of the impact of GAAR. Although Singapore has come down to the second position, foreign inflows from that country are increasing year after year. FDI inflow of USD 6.74 billion in 2014-15 was the highest ever received from Singapore since 2006-07. Though the government plays an active role in investment promotion the investment decisions of investors are based on the macro economic policy framework , investment climate in the host country , investment policies of the trans national corporations and other commercial considerations.

Section X

FIPB Sectoral Regulation-Entry Routs For India

The **foreign direct investment** in indian business sectors, can easily be made in a variety of ways, through the Governmental and Automatic Routes. However, the Joint Ventures are the most popular and preferred forms of making investment in Indian industry. At present, the most lucrative business sectors for FDI in India are, Infrastructure (Power, Steel, Railways, etc.); Telecommunications; Hospitality sector; Education; Retail; Real Estate; Retail sector, Petroleum and Petroleum Products; Biotechnology; Alternative Energy, etc. Investments can be made by non-residents in the equity shares/fully, compulsorily and Mandatorily convertible debentures/ fully, compulsorily and mandatorily convertible preference shares of an Indian company, through two routes;

1. The Automatic Route: under the Automatic Route, the non-resident investor or the Indian company does not require any approval from the RBI or Government of India for the investment. (NRI’s). The government reported move to do away with the Foreign Investment Promotion Board makes eminent sense. The board is set up in early 1990s to have an extra check to foreign ownership since sectoral rules were not robust. Rightly, successive governments have put more sectors under the automatic route and set up sectoral regulators for through oversight. Robust regulation obviates the need for the FIPB. Already, more than 90% of FDI is under the automatic route, and investors have to only inform the RBI. With a well developed corporate sector, a sound legal framework and huge economic potential, India remains one of the most attractive FDI destination. Making FDI approvals automatic would pay rich dividends.

2. The Government Route: under the Government Route, prior approval of the Government of India through Foreign Investment Promotion Board (FIPB) is required. Proposals for foreign investment under Government route as laid down in the FDI policy from time to time, are considered by the Foreign Investment Promotion Board (FIPB) in Department of Economic Affairs (DEA), Ministry of Finance.

Section XI
Role of Credit Rating Agency

Ratings agencies Standard & Poor's and Fitch have put India's sovereign credit rating on the watch citing poor economic fundamentals, high fiscal and current account deficits and lack of action from the government. A downgrade would take India's rating to below investment grade, which may force many investors to sell Indian securities or stop incremental investments, depressing capital flows and raising cost of borrowing for the local companies.

The recent slew of measures announced by the government, including FDI in multi-brand retail and diesel price hike, will support India's medium to long-term growth prospects. The measures will be a positive factor from a sovereign credit worthiness perspective for India..

Fitch Ratings will keep an eye on the implementation of the fiscal consolidation roadmap laid down by the Kelkar Committee report. The Reserve Bank of India's (RBI) ability to ease the monetary policy will be constrained by elevated inflation levels. Supply side factors will also keep RBI's hands tied. India's credit rating has partly been kept at a 'BBB-' owing to high fiscal deficit levels. India has higher fiscal deficit levels compared to other developing Asian countries.

Section XII
Double Taxation Avoidance Agreement (DTAA)

DTAA, is an agreement wherein, it allows the investor to pay tax in his resident nation , in this case **Mauritius,** so the corporations pay zero tax in Mauritius and get tax exemption in India. The reason for high investment is because, the money invested from Mauritius is nothing but the black money which was embezzled out of India via hawala transaction and laundered as tax free white money which our helpless government allows it to invest in India, for further scope of tax embezzlement and black money generation. It is popularly called as **the Mauritius route.** It is triply harmful to our Indian economy. A detailed examination is needed to find out if they constitute actual investments or whether they are diversions from other sources to avail tax benefits under the Double Taxation Avoidance Agreement (DTAA) that India has with these two countries.

Mauritius is a tax haven. Most of the investors who invest from Mauritius are not it's own citizens, but citizens of other nations who route their investment through Mauritius to cleverly avoid taxes. Recent example include Vodafone buying Hutch. The deal took place in Mauritius to avoid Indian taxes.

Mauritius dethroned by Singapore as top source of FDI into India

Mauritius has been dethroned by Singapore as the top source of Foreign Direct Investment (FDI) into India, with the Asia Pacific island economy accounting for 25% of FDI inflows into the emerging Asian economy in 2013-14. During the last financial year, India has attracted USD 4.85 billion in FDI from Mauritius compared to USD 5.98 billion from Singapore, according to data from the Department of Industrial Policy and Promotion (DIPP).

It may be noted that in the preceding financial year from April 2012 to March 2013, a healthy USD 9.49 billion was registered as FDI equity inflows to India from Mauritius, while for the same period, FDI equity inflows from Singapore to India stood at USD 2.31 billion. Thus, FDI from Mauritius to India has shrunk around 49% over the last year, while that from Singapore has increased by 159%. The reason behind this reversal of trend is the uncertainty over the Double Tax Avoidance Agreement (DTAA) between India and Mauritius. FDI inflows from Mauritius have started drying up on fears of the impact of General Anti Avoidance Rules (GAAR) and possible re-negotiation of the tax avoidance treaty.

Limit-of-Benefit (LoB) Clause

Conversely, according to experts, the Double Taxation Avoidance Agreement (DTAA) with Singapore incorporates the Limitation-of-Benefits (LoB) clause, which has provided comfort to foreign investors who increasingly prefer to use Singapore as a channel to route funds to India. According to tax experts in India, the LoB clause in India-Singapore treaty serves to justify the concept of economic substance in Singaporean entities, bringing certainty and avoiding chances of litigation. Incidentally, the inflows from Mauritius in the last fiscal are lowest since 2006-07. On the other hand, FDI inflow of USD 5.98 billion in 2013-14 is the highest ever received from Singapore since 2006-07. The India-Mauritius DTAA is being revised amid concerns that Mauritius is being used for round-tripping of funds into India even though that country has always maintained that there have been no concrete evidence of any such misuse.

Investors are performing Singapore to Mauritius as the LoB clause in India Singapore treaty provides substance and certainty. Overall , Singapore accounts for 15 percents of the total FDI India received between April 2015 and September 2015. However, Mauritius makes up 34 percent of FDI during the same period as shown in table 3.0 below.

Table 3.0

TRACKING FDI 2015

Top Source of FDI (April –Sept 2015)

Countries	**Rs**	**$ billion**
Singapore	43,096	6.7
Mauritius	23,490	3.7
Netherlands	7,017	1.2
Highest FDI equity inflow		
Computer*	19,504	3.0
Trading	14, 932	2.3
Services	9,404	1.5

Software and Hardware services sectors include banking, insurance, non financial /business , outsourcing, research and development, couriers, Research and Developments , Tech testing and analysis

Double Taxation Avoidance Agreement (DTAA) with Mauritius.

India signed the protocol amending the Double Taxation Avoidance Agreement (DTAA) with Mauritius. while the protocol gives India the right to tax capital gains arising from sale or transfer of shares of an Indian company acquired by a Mauritian tax resident, it proposes to exempt investments made until March 31, 2017, from such taxation. The government also said that shares acquired between April 1, 2017 and March 31, 2019 will attract capital gains tax at a 50% discount on the domestic tax rate — i.e., at 7.5% for listed equities and 20% for unlisted ones. The full tax impact of the protocol will fall on investments beginning April 1, 2019, when capital gains will attract tax at the full domestic rates of 15% and 40%. The DTAA was a major reason for a large number of foreign portfolio investors (FPI) and foreign entities to route their investments in India through Mauritius. Between April 2000 and December 2015, Mauritius accounted for $ 93.66 billion — or 33.7% — of the total foreign direct investment of $ 278 billion. The imposition of capital gains tax on the acquisition of shares of Indian companies after March 31, 2017 could, however, result in a slowing of the flow of investments.

Benefit as a result of the amendment

Netherlands may emerge as an attractive destination for FPIs following the changes to the Mauritius treaty. The India-Netherlands treaty is a smart treaty, and it can emerge as a preferred alternative for FIIs especially those in Europe. The treaty provides that if a company based in Netherlands holds less than 10% equity in an Indian entity, it would not attract capital gains on the sale of those shares to residents or non-residents. Even if it were to own more than 10% equity in an Indian company, the treaty allows it to sell the shares to a non-resident without attracting tax.

Section XIII

Investments through Participatory Notes (P-Notes)

There is no change in decision with regard to taxation of P-notes because of signing of the Mauritius treaty, P-Notes are instruments issued by registered foreign institutional investors to overseas investors. While the FPIs are registered with the Securities and Exchange Board of India (SEBI), the overseas investors investing in P-Notes are not registered with the market regulator, and thus their identity is not known to the authorities. SEBI's proposal to impose curb on P-notes on September 16, 2007, resulted in a sharp correction in the markets the following day, and forced the government to issue a clarification. Over the years, however, the share of P-notes in the total FPI investment has come down from around 50% in 2007 to 10% now.

Section-XIV
Global Opportunity Index

The index provides a systematic, data-rich framework to shed light on nations' attractiveness to foreign investors, the kind that commit "patient" capital to strategic projects that benefit all parties well into the future. It not only considers economic variables but also examines key business, legal, and regulatory policies that can drive those decisions.

The costs and conditions of doing business are central to the FDI equation. Natural resources and hardworking people have great value, of course, as do a sophisticated banking system and healthy industrial base. But countries that invest in their infrastructure, suppress corruption, and maintain sound regulations can claim important advantages. The Global Opportunity Index answers a pressing need for information that's vital to a thriving global economy. What policies can governments pursue to attract foreign direct investment (FDI), expand their economies, and accelerate job creation? What do multinational companies, other investors, and development agencies need to know before making large-scale, long-term capital commitments?

- Singapore, Hong Kong, and Finland achieved the highest scores. The top 10 are primarily economically advanced countries with longstanding institutions and traditions of transparency.
- Malaysia is the only developing country in the top 10 and is particularly strong in the Rule of Law.

Who's up and coming?

- Six sub-Saharan African countries — Mauritius, South Africa, Botswana, Rwanda, Namibia, and Zambia — are in the top 50 percent of the Index.
- Latin American nations the Dominican Republic, Colombia, and Guatemala were among the 10 most improved since 2007.
- In Latin America, countries with improving scores, including Chile, Uruguay, Panama, Colombia, and Ecuador, outnumbered those with declining scores by a 2-1 margin.
- From 2009 to 2015, there was a slight decline among many advanced economies and generally positive changes among developing countries, highlighting the hit that developed markets took during the financial crisis as well as continuing reforms in developing countries..
- Each one-unit increase in index score is associated with a 42 percent increase in FDI per capita and a 55 percent increase in international portfolio flows.

Section XV

Problems in FDI and Suggestions

Problems –

Physical infrastructure is the biggest hurdle that India currently faces, to the extent that regional differences in infrastructure concentrate FDI to only a few specific regions. While many of the issues that plague India in the aspects of telecommunications, highways and ports have been identified and remedied, the slow development of railways , water and sanitation continue to deter major investors.

Federal legislation is another perverse impediment for India .Local authorities in India are not part of the approval process and the large bureaucratic structure of the central government is often perceived as a breeding ground for corruption. Foreign investment is seen as a slow and inefficient way of doing business , especially in a paperwork system that is shrouded in red tape.

Suggestions

The government should allow free foreign investment except in critical areas of national interest and sensitive sectors such as the media. Sectoral FDI caps , varying between 49% and 74% across sectors as diverse as insurance, defence projects and banking, have only led to a policy mess, opening up a profitable market for Indian businessman to become a passive partner of overseas companies wanting to set up shop in India as holders of economic interest owned by the foreign party. Removing caps and allowing majority control by foreign partners in sectors such as insurance is the way to go.

The government should provide additional incentives to foreign investors to invest in states where the level of FDI inflows is quite low. Government should ensure the equitable distribution of inflows among low. states and must give more freedom to states, so that they can attract inflows at Government must target at attracting specific types of FDI their own level. that will be able to generate spillovers effects in the overall economy like investing in human capital, R&D activities, environmental issues, productive capacity, sectors with high income elasticity of demand.

The policy makers should focus more on attracting diverse types of FDI. and should design policies where foreign investment can be utilized as means of enhancing domestic production, savings, and exports and also as medium of technological learning and diffusion and also in providing access to the Government must exercise strict control over inefficient external market. bureaucracy, red - tapism, and the rampant corruption, so that investor's confidence can be maintained for attracting more FDI inflows to India.

Section XVI
Conclusion

Though the government plays an active role in investment promotion "the investment decisions of investors are based on the macro economic policy framework , investment climate in the host country , investment policies of the trans national corporations and other commercial considerations. To boost investment environment and attract foreign investments the government had brought in FDI related reforms and liberalized several major sectors.

References:

[1] The Hindu, May 28, 2016, pp-15
[2] The Hindustan Times, May 17, 2016, pp 12
[3] The Times of India, July 27, 2016, pp-16
[4] The Economic Times, November 19, 2013, pp13
[5] The Times of India, Feb 20, 2013, pp-12
[6] The Economic Times, March 19, 2014 , pp-16
[7] The Economic Times, October 4, 2012
[8] The Economic Times 24 Nov, 2013
[9] The Economic Times, July 28, 2014, pp-9
[10] The Times of India, July 12, 2014, pp-5
[11] The Times of India, July 30, 2016, pp-9
[12] The Economic Times, August 28, 2016, pp-1
[13] The Times of India June 7, 2016, pp10
[14] The Economic Times, Feb 8th 2017, pp 12
[15] The Economic Times, Feb 22, 2017, pp-15

x-x-x-x