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Foreign Direct Investment (FDI) in Selected Sectors - Issues and Concerns for India

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KEYWORDS

Most of the under developed countries suffer from low level of income and low level of capital accumulation. However despite this shortage of capital, these countries have developed a strong urge for industrialization and economic development. For instance, India launched upon an ambitious programme of industrialization during the second five year plan. Since the domestic recourses to carry out this programme were insufficient, the country had depend on foreign capital.

Foreign investment in India is governed by the FDI policy announced by the government of India and the provision of the Foreign Exchange Management Act (FEMA) 1999. Reserve Bank has issued notification No. FEMA 20/2000 RB dated May 3, 2000, which contains the regulation in this regard. This notification has been amended form time to time.

Foreign investment is freely permitted in almost all sectors. Under foreign direct investment scheme investments can be made by non-residents in the shares/ convertable debentures of an Indian company, under two routes:

- automatic route and
- Government route

Under the automatic route, the foreign investor the Indian company does not require any approval from the Reserve Bank or Government of India for the investment. Under the government route, prior approval of government of India, ministry of finance, Foreign Investment Promotion Board (FIPB) is required 1.

ELIGIBILITY FOR FOREIGN DIRECT INVESTMENT IN INDIA

A person resident outside India (other than a citizen of Pakistan or Bangladesh) or an entity incorporated outside India, (other than an entity incorporated in Pakistan or Bangladesh) can invest in India, subject to the FDI policy of the Government of India.

A person who is citizen of Bangladesh or an entity incorporated in Bangladesh can invest in Indian under the FDI scheme, with prior approval of FIPB.

Overseas corporate Bodies (OCBs) are entities Government approval, if any, have been complied with the company is eligible to issue shares under these Regulation and the company has all original certificates issued by authorized dealers in India evidencing receipt of amount of consideration. A certificate from Statutory Auditors or Chartered Accountant indicating the manner of arriving at the price of the shares issued to the persons resident outside India 2.

The report of receipt of consideration as well as FC-GPR has to be submitted to the concerned Regional office of the Reserve Bank under whose jurisdiction the registered office of the company is situated. Part B of FC-GPR should be fled on an annual basis by the Indian company directly with the Reserve Bank. This is an annual return to be submitted by 31st of July every year, pertaining to all investments by way of direct / portfolio investments re-invested earnings others in the Indian company made during the previous years (i.e. The information in part B submitted by 31st July, 2008 will pertain to all the investments made in the previous year's up to March 31, 2008). The details of the investments to be reported would include all foreign investments made into the company which is outstanding on the balance sheet date. The details of overseas investment in the company both under direct / portfolio investment may be separately indicated 3.

GUIDELINES FOR CONSIDERATION OF FDI PROPOSALS BY FIPB:

The following guidelines are laid down to enable the FIPB to consider the proposals for FDI and formulate its recommendations 4.

1. All applications should be put up before the FIPB by its Secretariat within 15 days and it should be ensured that comments of the administrative ministries are placed before the Board either prior to/or in the meeting of the Board.
2. Proposals should be considered by the Board keeping in view the time frame of thirty (30) days for communicating Government decision.
3. In cases in which either the proposal is not cleared or further information is required in order to obviate delays presentation by applicant in the meeting of the FIPB should be resorted to.
4. While considering cases and making recommendations, FIPB should keep in mind the sectoral requirements and the sectoral policies vis-à-vis the proposal (s).
5. FIPB would consider each proposal in its totality.
6. The Board should examine the following while considering proposals submitted to it for consideration:

(i) whether the items of activity involve industrial licence or not and if so the considerations for grant of industrial licence must be gone into;
(ii) whether the proposal involves any export projection and if so the items of export and the projected destinations;
(iii) Whether the proposal has any strategic or defence related considerations.

7. While considering proposals the following may be prioritized:

(i) Items falling in infrastructure sector;
(ii) Items which have an export potential;
(iii) Items which have large scale employment potential and especially for rural people;
(iv) Items which have a direct or backward linkage with agro business/farm sector;
(v) Items which have greater social relevance such as hospitals, human resource development, life saving drugs and equipment;
(vi) Proposals which result in induction of technology or infusion of capital.

8. The following should be especially considered during the scrutiny and consideration of proposals.

(i) The extent of foreign equity proposed to be held (keeping in view sectoral caps if any;

(ii) Extent of equity from the point of view whether the proposed project would amount to aholding company/wholly owned subsidiary/a company with dominant foreign investment (i.e. 76% or more) joint venture;
(iii) Whether the proposed foreign equity is for setting up a new project (joint venture or otherwise) or whether it is for enlargement of foreign/NRI equity or whether it is for fresh induction of foreign equity/NRI equity in an existing Indian company;
(iv) In the case of fresh induction offerings/NRI equity and/or in cases of enlargement of foreign/NRI equity, in existing Indian companies whether there is a resolution of the Board of Directors supporting the said induction/enlargement of foreign/NRI equity and whether there is a shareholders agreement or not;
(v) In the case of induction of fresh equity in the existing Indian companies and/or enlargement of foreign equity in existing Indian companies, the reason why the proposal has been made and the modality for induction/enhancement (i.e. whether by increase of paid up capital/authorized capital, transfer of shares (hostile or otherwise) whether by-rights issue, or by what modality;
(vi) Issue/transfer/pricing of shares will be as per SEBI/RBI guidelines;
(vii) Whether the activity is an industrial or a service activity or a combination of both;
(viii) Whether the items of activity involves any restriction by way of reservation for the Micro & Small Enterprises sector;
(ix) Whether there are any sectoral restrictions on the activity;
(x) Whether the proposal involves import of items which are either hazardous/banned or detrimental to environment (e.g. import of plastic scrap or recycled plastics).9.No condition specific to the letter of approval issued to a non-resident investor would be changed or additional condition imposed subsequent to the issue of a letter of approval. This would not prohibit changes in general policies and, regulations applicable to the industrial sector.

TOP INVESTING COUNTRIES FDI EQUITY INFLOWS Amount Rupees in crores (US$ in million)

Ranks	Country	2008-09 (April-March)	2009-10(April-March)	2010-11 (April- March)	Cumulative Inflows (April '00 - March '11)	%age to total Inflows (in terms of US $)
1	MAURITIUS	50,899(11,229)	49,633 (10,376)	31,855 (6,987)	242,761 (54,227)	42 %
2	SINGAPORE	15,727 (3,454)	11,295 (2,379)	7,730 (1,705)	52,876 (11,895)	9 %
3	U.S.A.	8,002 (1,802)	9,230 (1,943)	5,353 (1,170)	42,542 (9,449)	7 %
4	U.K.	3,840 (864)	3,094 (657)	3,434 (755)	29,433 (6,639)	5 %
5	NETHERLANDS	3,922 (883)	4,283 (899)	5,501 (1,213)	25,627 (5,700)	4 %
6	JAPAN	1,889 (405)	5,670 (1,183)	7,063 (1,562)	23,958 (5,276)	4 %
7	CYPRUS	5,983 (1,287)	7,728 (1,627)	4,171 (913)	21,948 (4,812)	4 %
8	GERMANY	2,750 (629)	2,980 (626)	908 (200)	13,376 (2,999)	2 %
9	FRANCE	2,098 (467)	1,437 (303)	3,349 (734)	10,267 (2,264)	2 %
10	U.A.E.	1,133 (257)	3,017 (629)	1,569 (341)	8,592 (1,890)	1 %
TOTAL FDI INFLOWS *		123,025 (27,331)	123,120 (25,834)	88,520 (19,427)	580,722 (129,716)	-

SECTORS ATTRACTING HIGHEST FDI EQUITY INFLOWS Amount in Rs. crores (US$ in million)

Ranks	Sector	2008-09	2009-10	2010-11	Cumulative Inflows	%age to total Inflows (in terms of US $)
1	SERVICES SECTOR(financial & non-financial)	28,516 (6,138)	20,776 (4,353)	15,539 (3,403)	120,771 (27,007)	21 %
2	COMPUTER SOFTWARE & HARDWARE	7,329 (1,677)	4,351 (919)	3,571 (784)	47,700 (10,723)	8 %
3	TELECOMMUNICATIONS (radio paging, cellular mobile, basic telephone services)	11,727 (2,558)	12,338 (2,554)	7,546 (1,665)	48,220 (10,589)	8 %
4	HOUSING & REAL ESTATE	12,621 (2,801)	13,586 (2,844)	5,149 (1,127)	43,192 (9,632)	7 %
5	CONSTRUCTION ACTIVITIES (including roads & highways)	8,792 (2,028)	13,516 (2,862)	5,077 (1,125)	40,770 (9,178)	7 %
6	AUTOMOBILE INDUSTRY	5,212 (1,152)	5,754 (1,208)	6,008 (1,331)	26,831 (5,927)	5 %
7	POWER	4,382 (985)	6,908 (1,437)	5,709 (1,252)	26,712 (5,900)	5 %
8	METALLURGICAL INDUSTRIES	4,157 (961)	1,935 (407)	5,055 (1,105)	18,495 (4,235)	3 %
9	PETROLEUM & NATURAL GAS	1,931(412)	1,328 (272)	2,621 (574)	13,735 (3,153)	2 %
10	CHEMICALS(other than fertilizers)	3,427(749)	1,707 (362)	1,810 (398)	13,078 (2,892)	2 %

SECTORAL CAP ON INVESTMENT BY PERSON RESIDENT OUTSIDE INDIA

S.No	Sector	Investment Cap	Description of Activity/ Items / Conditions
1	Private Sector Banking	74%	Subject to guidelines issued by RBI banking from time to time.
	Non-Banking Financial Companies	100%	FDI/ NRI investments allowed in the following 18 NBFC activities shall be as per the levels indicated below:
			(a) Activities covered
			1. Merchant Banking 2. Under writing 3. Portfolio Management Services 4. Investment Advisory Services 5. Financial Consultancy 6. Stock broking 7. Asset Management 8. Venture Capital 9. Custodial Services 10. Factoring 11. Credit Rating Agencies 12. Leasing & Finance 13. Housing Finance 14. Forex Broking 15. Credit Card Business 16. Money changing Business 17. Micro Credit 18. Rural Credit
			(b) Minimum capitalization norms for fund based NBFCs
			1. For FDI upto 51% US$ 0.5 million to be brought in upfront. 2. If the FDI is above 51% & upto 75% US $5 million to be brought upfront. 3. If the FDI is above 75% and upto 100% , US$ 50 million out of which $7.5 million to be brought in upfront and the balance in 24 months
2	Insurance	26%	FDI upto 26% in the Insurance sector is allowed on the automatic route subject to obtaining license from Insurance Regulatory & Development Authority.
3	Venture Capital Fund (VCF) and Venture Capital Company (VCC)		Offshore Venture Capital Funds / companies are allowed to invest in domestic venture Capital undertaking as well as other companies through automatic route, subject to only SEBI regulations and sector specific caps on FDI.
4	Trading		Trading is permitted under automatic route with FDI upto 51% provided it is primarily export activities, and the undertaking is an export house/ trading house/ star trading house/ super trading house. However, under the FIPB route.
S.No	Sector	Investment Cap	Description of Activity/ Items / Conditions
5	Hotel & Tourism	100%	The term hotels include restaurants, beach resorts and other tourist complexes providing accommodation and / or catering and food facilities to tourists. Tourism related industry include travel agencies, tour operating agencies and tourist transport operating agencies, units providing facilities for cultural, adventure and wild life experience to tourists, surface, air and water transport facilities to tourists, leisure, entertainment, amusement, sports and health units leisure, entertainment, amusement, sports and health units for tourists and Convention / Seminar units and organizations.
			For foreign technology agreements, automatic approval is granted if
			(i) Upto 3% of the capital cost of the project is proposed to be paid for technical and consultancy.
			(ii) Upto 3% of the net turnover is payable for franchising and marketing / publicity support fee, and Upto 10% of gross operating profit is payable for management fee, including incentive fee.
6	Special Economic Zones	100%	All manufacturing activities excepts: (i) Arms and ammunition, Explosives and allied items of Defence equipments, Defence aircrafts and warships. (ii) Atomic substances, Narcotics and Psychotropic Substances and hazardous Chemicals, (iii) Distillation and brewing of Alcoholic drinks and (iv) Cigarette / cigars and manufactured tobacco substitute.

Conclusion

In absolute terms, India has received a large amount of foreign aid for development purposes during the past five and a half decades. However, its position is not enviable if we consider the amount of aid in relation to its population. During the First Plan period, India had received on an average an external assistance of Rs.40 crore per annum. This was certainly a modest amount by any standards. Thereafter, for more than a decade there was a steady increase in external assistance. During the Third Plan period, this country received, on an average, an external assistance of Rs.573.3 crore per annum, which was 3.2 per cenet of national income. After the Third Plan was over, the long-term planning was suspended for three years. As the country's economy was in a bad shape in this period and it was not easy to raise adequate resources from domestic sources, reliance on foreign and increased during the three years of Annual Plans. However, the Fourth Plan marked a distinct change in the pattern of finance. This change was induced basically by two reasons: (i) because of the increasing certainty of aid and the rising debt servicing charges, the Government of India opted for a policy of increasing self-reliance. Under the Fifth Five Year Plan, self-reliance was again accorded a high priority and thus the aid received for the plan in percentage terms was approximately on the same scale as under the Fourth Plan. The Sixth Plan envisaged a net inflow of foreign resources of Rs.9,929 crore (Rs.5.889 crore as net aid and Rs.4,040 crore as other inflows from abroad). This was about 10.2 per cent of the total public sector plan outlay of Rs.97,500 crore. The Seventh plan envisaged net capital inflow from abroad of

Rs.18,000 crore which was again 10 per cent of the public sector plan outlay of Rs.1,80,000 crore. The Eighth Plan reduced the contribution of net capital inflow from abroad to 6.6 per cent (Rs.28,700 core out of the total public sector outlay of Rs.4,34,100 crore). The actual dependence on foreign aid was still less at 5 per cent in the Eighth Plan (Rs.19,234 crore out of the total of Rs.3,80,524 crore) at 1991-92 prices. The share of net inflow from abroad in the Ninth Plan was kept at 7 per cent (Rs.60,018 crore out of Rs.8,59,200 crore. The Tenth Plan aimed to reduce the dependence on net inflow from abroad considerably. Only Rs.27,200 crore out of the total Central Plan outlay of Rs.9,21,291 crore (just 3.9 per cent at 2001-02 prices) was planned to be raised through this means. The actual dependence on net inflows from abroad was still lower at Rs.12,966 crore (which was only 2.2 per cent of total Central Plan expenditure of Rs.7,60,327 crore). The Eleventh Plan keeps no provision for net inflows from abroad.

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