Transit to the 5 Trillion Dollar Economy – Further liberalisation of FDI norms.

written by Pawan Khatri | August 30, 2019

The much-awaited fillip required to propel the flagging economy came in the form of approval from the Cabinet Committee on Economic Affairs which on 28th August, 2019 approved changes to FDI policy post assurances made in the recent Budget speech. The changes in FDI policy across four sectors include foreign investment in digital media up to 26%, 100% foreign direct investment for coal mining and contract manufacturing and easing of sourcing norms for single-brand retailers.

In the wake of Global FDI inflows facing headwinds over the last few years, there has been a lot of push towards further liberalising norms in these sectors and the Government has opened doors acknowledging the value of the single largest source of non-debt finance that the economy is in dire need of.

Let's take a look at the nuts and bolts of what this means to foreign investors and the economy as a whole sector-wise.

FDI in Single Brand Retail Trading (SBRT)

- Strict sourcing norms that were previously prevalent have been whittled down and SBRT entities having more than 51% FDI can now manage their 30% sourcing requirement irrespective of whether the sourcing is done for local or global operations.
- Sourcing of goods from India for global operations can be done both directly or indirectly through a legally tenable agreement which was previously not possible through unrelated third parties.
- The requirement of SBRT entities that were previously not permitted to initiate trading via online stores without opening brick and mortar stores has also been done away with.

Impact:

Providing clarity and easing up sourcing norms is expected to bring in fence-sitters who have been waiting on the sidelines for the Government to ease the FDI norms.However,not addressing multi-brand retail is a big miss and foreign retailers selling a wide range of product categories would have to continue sitting on the fence. On the positive side, given that the Government has already tested waters in retail, easing of norms is expected to further enhance the 'Make in India' brand globally and enhance domestic production. Given the complex nature and dynamics of the Indian market, it is unlikely that most of the large retailers would sail by themselves and we are likely to see partnerships foster dispelling any concerns for large Indian groups.

This also augurs well for foreign retail entities who were skeptical about entering the Indian market earlier due to high investment requirement of setting up brick and mortar stores and can now test the waters by starting to trade through online stores without opening brick and mortar stores at least for a period of two years.

FDI in Coal Mining

As on 31 March 2018, India had 319.04 billion metric tons (351.68 billion short tons) of coal and despite burgeoning demand, Coal India which has the monopoly to exploit resources has under-delivered and India has had to import this coal deficit despite having the 5th largest reserves in the world. 100% FDI via automatic route is a welcome step in the right direction for the commercial exploitation of coal and other ancillary operations. This liberalisation in the coal sector paves way for bringing in newer technologies in coal extraction and ending the sole dominance of Coal India.

Impact:

There are several challenges that remain despite the opening up of FDI in coal. Amongst others, the three-headed hydra namely environment clearances, mining leases and land acquisition have to be dealt with if foreign investors are to be interested in coal mining which is a highly capital-intensive industry. The process of auction of mining leases may also have to be tweaked into two stages namely price discovery and allotment based on a first-come basis through a thorough process of diligence. Clear process in environment clearances along with set procedures for land acquisitions will be some of the minimum guarantees that a foreign investor would look at while exploring coal.

Contract Manufacturing

Though existing norms permit 100% FDI in the manufacturing sector under the automatic route, there is no clarity on contract manufacturing. This has now been clarified and 100% FDI under automatic route has now been allowed in contract manufacturing by any entity for investment and manufacturing through a contract either on both Principal to Principal and Principal to Agent basis.

Impact:

Contract manufacturing is expected to provide a major fillip to the Indian economy and create more employment opportunities. Sectors including electronics and pharma which avail the tool of contract manufacturing will be keen to exploit the Indian market. Given the backdrop of the US-China trade war, this move can perhaps work to India’s benefit as American

companies
facing the heat from China look to greener pastures.

FDI in Digital Media

The existing FDI policy was silent on FDI in Digital Media and the proposal to permit 26% FDI under government route has now been permitted for entities undertaking uploading/ streaming of News & Current Affairs through Digital Media.

Impact:

FDI in Digital Media may perhaps be a double-edged sword and further clarity is required on what constitutes Digital Media since this was largely looked at as a sub-set of broadcasting entities where the previous policy provided 49% FDI in broadcasting and has enabled some broadcasting houses having 49% FDI to also have a digital arm which as specified could undertake “uploading/ streaming of news & current affairs through Digital Media”. However, this change in FDI policy can land a number of media entities in a spot of bother and is perhaps a regressive move considering 49% FDI in television. The treatment of foreign news sites will also have to be clarified since it virtually not possible to ban sites that are non-compliant.

Despite some misses, the changes in FDI policy are in the right direction and should provide the necessary shot in the arm for the Indian economy and drive up consumption and investments further augmenting the perception of Indian growth story globally.

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