Barriers to FDI in India

A stark contrast is observed on the status of Indian economy between the period August and May 2015 in a scenario which reflects falling global crude oil prices , falling interest rates in most of the developed and developing countries, and a major economy like China undergoing economic depression. The good news, India being complimented for its good economic health with inflation falling by 4-5% levels and the current account expected to be at near balance in the current year and this supports well for the stability of the INR. The RBI projects January-March inflation to be lower by 0.2%, i.e 5.8% rather than 6% . Though the economic variables exhibit sound projections, compliments cannot be taken seriously until the manufacturing sector truly shows a boom. Higher interest have still being held in order to have an attractive FDI climate, however in today's scenario, the observed status of FDI investment is nothing different from the one in 2013 thanks to the barriers still being in place. The Indian government is taking numerous steps to boost investment as well as reviving stalled projects and infusing more capital into public sector banks. Though these measures are being taken, India is being still short sold in the International business environment without any underlying attempt made to remove the barriers to the entry and free access of FDI capital in the country.

The existing barriers to FDI are:

Restrictive FDI regime
The FDI regime in India is still quite restrictive. As a consequence, with regard to crossborder ventures, India ranks 57th in the GCR 1999. Foreign ownership of between 51 and 100 percent of equity still requires a long procedure of governmental approval. In our view, there does not seem to be any justification for continuing with this rule.

Lack of clear cut and transparent sectoral policies for FDI
Expeditious translation of approved FDI into actual investment would require more transparent sectoral policies, and a drastic reduction in time-consuming red-tapism.

High tariff rates by international standards
India's tariff rates are still among the highest in the world, and continue to block India's attractiveness as an export platform for labor-intensive manufacturing production. On tariffs and quotas, India is ranked 52nd in the 1999 GCR, and on average tariff rate, India is ranked 59th out of 59 countries being ranked.

Lack of decision-making authority with the state governments
The reform process so far has mainly concentrated at the central level. India has yet to free up its state governments sufficiently so that they can add much greater dynamism to the reforms. In most key infrastructure areas, the central government remains in control, or at least with veto over state actions. Greater freedom to the states will help foster greater competition among themselves.

Limited scale of export processing zones
The very modest contributions of India's export processing zones to attracting FDI and overall export development call for a revision of policy. India's export processing zones have lacked dynamism because of several reasons, such as their relatively limited scale.

No liberalization in exit barriers
While the reforms implemented so far have helped remove the entry barriers, the liberalization of exit barriers has yet to take place

Stringent labor laws
Large firms in India are not allowed to retrench or layoff any workers, or close down the unit without the permission of the state government. Most importantly, the continuing barrier to the dismissal of unwanted workers in Indian establishments with 100 or more employees paralyzes firms in hiring new workers. Labor-intensive manufacturing exports require competitive and flexible enterprises that can vary their employment according to changes in market demand and changes in technology, so India remains an unattractive base for such production in part because of the continuing obstacles to flexible management of the labor force.

Financial sector reforms Reform of India's financial sector is crucial for large FDI flows into India. However, only some partial steps have been undertaken and these are by no means going to make any meaningful changes to the existing system. India's banking and insurance companies were nationalized more than two decades ago.
High corporate tax rates corporate tax rates in East Asia are generally in the range of 15 to 30 percent, compared with a rate of 48 percent for foreign companies in India. High corporate tax rate is definitely a major disincentive to foreign corporate investment in India. With respect to tax evasion, India is ranked 48th in the GCR 1999.

As a general rule, a country with a consistently lower inflation rate exhibits a rising currency value, as its purchasing power increases relative to other currencies. India has been showing a negative growth in inflation rate with decrease in WPI levels and hence the Indian rupee has appreciated quickly in response to the global scenario and decreasing inflation characteristics. The fiscal deficit scenario too has shown a meltdown displaying a near negative trend in current account. Though these news trends are impressive as compared to the same a year before , it should be noted that a higher currency makes a country's exports more expensive and imports cheaper in foreign markets. Interest rates, inflation and exchange rates are all highly correlated. By manipulating interest rates, central banks exert influence over both inflation and exchange rates, and changing interest rates impact inflation and currency values. Higher interest rates offer lenders in an economy a higher return relative to other countries. Therefore, higher interest rates attract foreign capital and cause the exchange rate to rise. In the present economic scenario though an emphasis has been made to attract foreign investment, the same is not happening on a full fledged basis. India's continuing ambivalence to FDI, as a result, exacts a heavy toll on the Indian economy. Undoubtedly, India is ceding billions of dollars of FDI to its neighbors each year, flows that otherwise would have come to India. Why is it that India, which provides the largest market after China in the developing world is unable to attract substantial volume of FDI? Given that India has a huge domestic market and a fast growing one, there is every reason to believe that with continued reforms that improve institutions and economic policies, and thereby create an environment conducive for private investment and economic growth that substantially large volumes of FDI will flow to India.

There is no doubt that foreign investment in form of FDI is a long term non- volatile investment which will boost not only employment but also will lead to growth in manufacturing sector and export led growth. However, the expected outcome of keeping the interest rates is not helping the manufacturing sector to grow and neither is the expected FDI pouring in. The manufacturing sector is in thirst of low interest capital to feed their working capital requirements or seek the restructuring of bad loans to avoid insolvency or increase their export competitiveness.

With the Chinese economy slowing down, India has the opportunity to become the global manufacturing hub and the target to achieve 8% growth rate is not non achievable.

In a climate struck with high inflation levels, high fiscal deficit and low growth it was imperative to hold a high interest rate regime and maintain the present FDI flows as well as bring the economy under control. However, it is seriously proposed that the government should now implement an interest rate cut or deploy a subsidy framework to the manufacture sector to ease out its needs so that there is a sign of positive growth in the industry. The latter proposed subsidy infr5astructure will further immunize the economy and maintain a balance between the needs of availability of capital at lower interest rate and provide the best returns on proposed pension and insurance funds.