Business Financing for Foreign Investors in India

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Address by Mr. Rakesh Shah, Chairman, EEPC India

It is a privilege to be in the midst of this distinguished gathering to share some thoughts on business financing for foreign investors in India. I must thank the National SME Council of Malaysia for organizing this event which is most appropriate for those wishing to invest in India.

Let me begin with a quote from India's Commerce & Industry Minister Mr. Kamal Nath. Mr. Nath said and I quote *"a decade and half ago the prospect of India becoming a major player in the global economy seemed a distant dream, only a theoretical possibility. During the last 14 years there has been a sea change not only in the world's perception about India's future, but in our own perception about ourselves. The world has acknowledged the "arrival of India". We no longer discuss the future of India: we say the future is India".* Unquote.

Ladies and Gentlemen, India is the largest democracy and the 4th largest economy (in terms of PPP) in the world. India is also the tenth most industrialized country in the world. With its consistent growth performance and abundant high-skilled manpower, India provides enormous opportunities for investment, both domestic and foreign. Since the beginning of economic reforms in 1991, major reform initiatives have been taken in the fields of investment, trade, financial sector, exchange control simplification of procedures, enactment of competition and amendments in the intellectual property rights. India provides a liberal, attractive and investor friendly investment climate.

☑ Potential in India

Today, India presents a vast potential for overseas investment and is actively encouraging the entrance of foreign players into the market. No company, of any size, aspiring to be a global player can, for long, ignore India which is expected to become one of the top three emerging economies. India has among the most liberal and transparent policies on FDI among the emerging economies. FDI up to 100% is allowed under the automatic route all activities and areas except in a few sensitive areas.

☑ Entry Options

What are the entry options for a foreign investor into India? There are basically two modes of entering India. The most commonly used method is in terms of entering as an “incorporated entity” under the Indian Companies Act. Thus, a foreign investor could choose to enter either as a Joint Venture or wholly owned subsidiary. Foreign equity in such an Indian company could be up to 100% depending upon the requirements of the investor, subject to any equity caps prescribed in respect of the areas of activities under the FDI policy.

The other method could be to enter as an “unincorporated entity” in the form of either a Liaison or Representative Office, or a Project Office or even a Branch Office. There are specific guidelines laid down by India’s Central Bank, the RBI for such unincorporated entities.

☑ **Financing Routes and Approval Methods**

With respect to the financing of Foreign direct investment, via the incorporated route is concerned, the following options are available to foreign investor:

- Through financial collaborations;
- Through joint ventures and technical collaborations;
- Through capital markets via Euro issues; and
- Through private placements or preferential allotments

I must also add that there are two varieties of FDI approvals in India. Under the automatic route, the FDI in sectors and activities permitted does not require any approval either by the Government or the RBI. The investors are only required to notify the Regional Offices of the concerned RBI within 30 days of receipt of inward remittances and file the required documents with that office within 30 days of issue of shares to the foreign investors.

However for areas or activities which are not covered under the automatic route, prior approval of the Government is required. Such proposals are considered by the Foreign Investment Promotion Board (FIPB). The FIPB is an extremely efficient body and meets regularly to approve or reject investment proposals submitted before it.

I must also draw attention to a couple of salient features of Indian FDI policy with respect to financing methods and flexibility. These are:

- India allows free repatriation of capital investment and profits thereon, provided the original investment was made in convertible foreign exchange;
- Use of foreign brand names and trademarks are for the sale of goods are allowed in India;
- Indian capital markets are open to Foreign Institutional Investments (FIIs); and
- Indian companies are allowed to raise funds from international capital markets.

☑ Foreign Technology Agreements

The RBI accords automatic approval to foreign technology agreements in all industries within certain monetary limits. Thus, technical know-how fees, payments for design and drawings, payment for engineering services and other royalty payments are acknowledged to be part foreign technology agreements.

☑ Foreign Portfolio Investments

With respect to Foreign Portfolio Investments, FIIs must register themselves with India’s Securities Exchange Board of India or SEBI and comply with the exchange control regulations of the RBI. Thus, India allows Foreign Pension Funds, Mutual Funds, investment trusts, asset management companies, nominee companies, and incorporated/institutional portfolio managers or their power of attorney holders to invest in India as FIIs. FIIs are allowed to invest in securities traded in primary and secondary capital markets in India under the portfolio investment scheme. These include shares, debentures, warrants, units of mutual funds, government securities and derivative instruments.

☑ ADRs/GDRs/FCCBs

Another important area of financing is the ADRs/GDRs/ FCCB route for qualifying Indian companies. Thus, these Indian companies can raise foreign equity through either of these routes which would form part of the FDI equity caps. This apart, there is the choice of investing in India through the preference share route. Foreign investment through convertible preference shares is treated as FDI. These investments can be made either through the automatic route or the Government approval route.

☑ ECBs

Finally, India also allows External Commercial Borrowings (ECBs), for qualified Indian companies. Debts raised in foreign currency fall within the definition of ECBs, and are regulated by India's Ministry of Finance and the RBI. ECBs can be approved through the automatic route as well as the approval route. ECBs can be availed by corporates registered under the Indian Companies Act except for financial intermediaries and must be availed from an internationally recognized source, export credit agencies, suppliers of equipment, foreign collaborators and foreign equity holders.

☑ **FDI in Small Scale Sector**

The current FDI norms impose a ceiling of 24 per cent FDI for companies in the SSI sector i.e. small scale units having capital investment in plant and machinery not exceeding USD 1,250,000 (Rs. 50,000,000). With a view to liberalizing the SSI sector and augmenting economic activity in the country, the Indian Government is likely to relax the FDI norms governing SSIs. According to government data, there are about 12.8 million small & medium enterprises in India, which produce goods worth over $140 billion. These Companies also export goods worth $33 billion (only SSI, excluding medium scale), accounting for around a third of India's total exports.

When the FDI limits are raised, SSI units would be eligible to raise foreign equity in accordance with caps governing the sectors in which they operate, thereby improving their access to technology and capital and assisting in the growth and modernization of the sector.

☑ **India's Banking and Judicial System**

As is, therefore, obvious there are a plethora of financing options for making investments into India. India's financial system is fairly well developed with 28 public sector banks led by the State Bank of India, 28 private sector banks, 29 foreign banks, co-operative banks, Regional Rural banks and a spate of Non-Banking Financial Institutions. This apart, there are other specialized agencies like the

EXIM Bank of India, the Export Credit Guarantee Corporation, the Small Industries Development Bank of India (SIDBI) catering to specific needs of exporters and the small scale sector.

Further, India's has a three tier judicial system with the Supreme Court of India being the Apex court of the country, followed by the High Courts in different States of the Country and below them lies the sub-ordinate courts where most cases originate.

I have attempted to give a bird's eye view of the possible avenues of financing foreign investment in India. The EEPC India can always be contacted for any further details and I would urge you to check our website www.eepcindia.org for the various contact points where foreign investors may tap to seek any information pertaining to doing trade and investment in India.

Thank you.