2. India Eases FDI Norms for Foreign Companies with Limited Chinese Shareholding – Economy

1. Why in News

1. Government of India has amended rules under the Foreign Exchange Management Act (FEMA) to ease Foreign Direct Investment (FDI) norms
2. Relaxation specifically targets foreign companies with limited Chinese shareholding
3. Amendment introduces the concept of "beneficial ownership" threshold of 10% for Chinese stakes
4. Move aims to balance national security concerns with need for foreign investment
5. Reflects pragmatic approach to foreign investment policy amid evolving geopolitical landscape
6. Expected to boost FDI inflows while maintaining strategic safeguards

Context and Background

1. Department for Promotion of Industry and Internal Trade (DPIIT) mandated strict FDI rules in 2020
2. Earlier framework required prior government approval for any level of investment from countries sharing land border with India
3. Rule applied even if Chinese shareholding was minimal or indirect
4. This created investment bottlenecks and affected companies with incidental Chinese exposure
5. New policy recognizes difference between strategic control and passive minority shareholding
6. Amendment provides clarity and predictability for foreign investors
7. Aligns with India's objective of becoming attractive investment destination

2. Earlier Framework and Its Limitations

Stringent Approval Requirements

1. Any level of investment from bordering countries required mandatory prior government approval
2. Applied to all sectors regardless of strategic sensitivity
3. Even minimal shareholding (less than 1%) triggered approval requirement
4. Created compliance burden for genuine foreign investors with incidental Chinese stakes
5. Delayed investment decisions and created uncertainty
6. Affected global companies with diverse shareholder base including minor Chinese participation

Broad Interpretation of Border Country Investment

1. Countries sharing land border with India include China, Pakistan, Bangladesh, Nepal, Bhutan, Myanmar, Afghanistan
2. Rule primarily aimed at Chinese investments following border tensions
3. However, blanket approach affected legitimate investments
4. Many global companies have Chinese institutional investors in small percentages
5. This indirect exposure brought them under approval route unnecessarily
6. Created disincentive for foreign portfolio investments

Impact on Investment Climate

1. Slowed down investment approvals and project implementation
2. Created regulatory uncertainty for foreign investors
3. Affected sectors needing quick capital infusion
4. Genuine investors deterred due to lengthy approval processes
5. India's competitiveness as investment destination impacted
6. Need felt for calibrated approach balancing security and investment

3. Revised Policy - Key Provisions

Concept of Beneficial Ownership

1. Amendment introduces threshold-based approach using "beneficial owner" concept
2. Definition derived from Prevention of Money Laundering Act (PMLA), 2002

3. Beneficial owner defined as person or entity having more than 10% ownership, control, or entitlement to profits
4. Focus shifts from any shareholding to significant beneficial ownership
5. Provides clear quantitative threshold for determining restrictions
6. Aligns with international anti-money laundering standards

Automatic Route for Limited Chinese Stake

1. Foreign companies with up to 10% Chinese or Hong Kong shareholding can now invest under automatic route
2. No prior government approval needed if Chinese stake below 10% threshold
3. Applicable subject to sectoral conditions where FDI already permitted on automatic route
4. Significantly simplifies investment process for majority of foreign companies
5. Reduces regulatory burden and approval timelines
6. Encourages global companies with minor Chinese exposure to invest

Exclusion of Bordering Country Entities

1. Relaxed norms do not apply to entities incorporated in China or Hong Kong
2. Entities incorporated in countries sharing land border with India also excluded
3. Such entities continue to require prior government approval regardless of ownership structure
4. Ensures direct investments from border countries remain under scrutiny
5. Maintains national security safeguards for sensitive investments
6. Targets indirect investments through third countries, not direct Chinese companies

Special Treatment for Multilateral Institutions

1. Investments by multilateral institutions where India is member not treated as investments from any specific country
2. Includes institutions like Asian Development Bank, World Bank, International Finance Corporation
3. Even if these institutions have Chinese participation, their investments exempt from border country restrictions
4. Recognizes multilateral nature and governance structure of such institutions
5. Facilitates access to development finance without geopolitical constraints

Reporting Requirements

1. Investments falling under relaxed category still subject to reporting requirements
2. Reserve Bank of India (RBI) prescribes reporting norms
3. Ensures regulatory oversight and monitoring of investment flows
4. Maintains transparency in foreign investment data
5. Allows government to track beneficial ownership patterns
6. Enables policy adjustments based on investment trends

4. Understanding Foreign Exchange Management Act (FEMA), 1999

Genesis and Objective

1. FEMA enacted in 1999 by Government of India
2. Replaced the Foreign Exchange Regulation Act (FERA), 1973
3. FERA was restrictive and prosecution-oriented
4. FEMA is facilitative and development-oriented
5. Aims to regulate foreign exchange transactions
6. Facilitates external trade and payments
7. Supports liberalization of Indian economy

Scope and Coverage

1. Provides legal framework for foreign exchange management in India
2. Covers Foreign Direct Investment (FDI) regulations
3. Regulates external commercial borrowings

4. Governs cross-border payments and remittances
5. Covers foreign portfolio investments
6. Regulates export and import of currency
7. Oversees foreign exchange holdings by residents

Regulatory Authority

1. Reserve Bank of India (RBI) is main authority implementing FEMA
2. RBI issues regulations, directions, and circulars under FEMA
3. Monitors compliance and enforces provisions
4. Grants approvals for transactions requiring permission
5. Investigates violations and imposes penalties
6. Works with other agencies like Enforcement Directorate for serious violations

5. Recent Trends in FDI Inflows to India

Overall Growth Trajectory

1. India's total FDI inflows including reinvested earnings increased to USD 88.29 billion during April-February 2025-26
2. Demonstrates sustained investor confidence in Indian economy
3. Growth despite global economic uncertainties and geopolitical tensions
4. Reflects success of government's investment promotion initiatives
5. Positions India among top FDI destinations globally

Investment Facilitation Achievements

1. Invest India (national investment promotion agency) facilitated grounding of 60 investment projects
2. Combined value exceeds USD 6.1 billion during 2025-26
3. Demonstrates effective investment facilitation mechanisms
4. Projects span diverse sectors and geographies
5. Reflects improved ease of doing business

Geographical Sources of Investment

1. Around 42% of total grounded investment value originates from European countries
2. Indicates strong engagement with developed economies
3. Top FDI source countries include Singapore, United States, Mauritius, UAE
4. Singapore remains largest source due to favorable tax treaty and business hub status
5. US investments focus on technology and services sectors
6. Mauritius used for investment routing due to treaty benefits
7. UAE investments growing in infrastructure and real estate

6. Sectoral Distribution of Investments

Dominant Sectors -

1. Pharmaceuticals sector attracting significant FDI due to India's manufacturing capabilities
2. Biotechnology sector benefiting from India's skilled workforce and R&D capabilities
3. Food processing sector growing with rising consumption and government support

Sunrise Sectors -

1. Electronics System Design and Manufacturing (ESDM) receiving focus under Production Linked Incentive scheme
2. Aerospace and defence sector opening up with increased FDI limits and Make in India push
3. Automobiles and Electric Vehicles (EVs) attracting investments for future mobility solutions

7. Understanding Foreign Direct Investment (FDI)

Definition and Nature

1. FDI refers to investments made by foreign entities in business interests of another country
2. Typically involves ownership or control of enterprises
3. Distinguished from Foreign Portfolio Investment (FPI) which is passive investment in securities

4. FDI involves long-term commitment and active participation in management
5. Can take forms including greenfield investments, brownfield investments, mergers and acquisitions

Prohibited Sectors

1. At present, FDI prohibited in specific sectors due to social, security, or policy reasons
2. Lottery business - social concerns and state monopoly
3. Gambling and betting - moral and social considerations
4. Chit funds - to protect small investors
5. Nidhi company - reserve cooperative character
6. Real estate business - except permitted categories like construction development
7. Manufacturing of cigars, cheroots, cigarillos and cigarettes using tobacco - health policy

Restricted Sectors

1. Some sectors have FDI caps limiting foreign ownership
2. Broadcasting sector - maximum 49% with conditions
3. Print media - 26% for newspapers, 100% for scientific magazines
4. Multi-brand retail - not permitted; single-brand retail 100% with conditions
5. Defence manufacturing - up to 100% with government approval beyond 74%
6. Banking - complex structure with sectoral limits

8. Routes for FDI in India

Automatic Route

1. No prior approval required from government or RBI
2. Investors need to inform RBI after making investment within specified timeframe
3. Most sectors fall under this route including manufacturing, IT, software
4. Facilitates quick capital infusion
5. Reduces regulatory burden and approval delays
6. Subject to sectoral caps and conditions where applicable
7. Post-investment reporting ensures regulatory oversight

Government Approval Route

1. Requires prior approval from concerned Ministry or Department
2. Foreign Investment Facilitation Portal (FIFP) used for applications
3. Sectors include telecom, media, pharmaceuticals (beyond certain limits), insurance
4. Also applies to investments from countries sharing land border
5. Approval based on multiple criteria including national security, sectoral policy
6. Timelines specified for processing applications
7. Rejections subject to appeal mechanisms

9. Significance of the Amendment

Balancing Security and Investment

1. Amendment strikes balance between national security concerns and investment needs
2. Maintains scrutiny on direct Chinese investments while facilitating global capital
3. Recognizes that blanket restrictions hurt India's investment competitiveness
4. Pragmatic approach addressing geopolitical realities without closing economy

Attracting Global Capital

1. Many multinational companies have diverse shareholder base including minor Chinese stakes
2. Earlier rules deterred such companies despite limited Chinese influence
3. Relaxation enables these companies to invest without approval delays
4. Improves India's attractiveness as investment destination
5. Competes better with other emerging markets for global capital

Sectoral Impact

1. Technology sector particularly benefits as global tech companies often have Chinese investors

2. Startup ecosystem gains as venture capital funds with minor Chinese participation can invest freely
3. Manufacturing sector benefits from easier access to global supply chain participants
4. Green energy and electric vehicle sectors can attract diverse international investors

Regulatory Clarity

1. Clear 10% threshold provides certainty to investors
2. Reduces subjective interpretations and discretionary approvals
3. Aligns with international standards on beneficial ownership
4. Improves predictability of investment regime
5. Facilitates compliance and reduces administrative costs

10. Challenges and Concerns

National Security Considerations

1. Need to ensure 10% threshold adequate to prevent strategic influence
2. Monitoring beneficial ownership requires robust institutional capacity
3. Shell companies and complex structures can obscure true ownership
4. Technology transfer and intellectual property protection remain concerns
5. Dual-use technologies require continued vigilance

Implementation and Monitoring

1. Effective reporting mechanisms needed to track beneficial ownership
2. Inter-agency coordination between DPIIT, RBI, intelligence agencies essential
3. Need for real-time monitoring of ownership changes
4. Capacity building for analysing complex corporate structures
5. Periodic review of threshold based on emerging patterns

Geopolitical Dynamics

1. China may view relaxation as insufficient or discriminatory
2. Border tensions and strategic competition continue
3. Need to balance economic engagement with security imperatives
4. Allies and partners' expectations regarding China policy
5. Domestic political sensitivities around Chinese investments

11. Way Forward

Ensuring Policy Stability

1. Continue providing stable, transparent, and investor-friendly regulations
2. Avoid frequent policy changes creating uncertainty
3. Maintain consistency in interpretation and implementation
4. Build investor confidence through predictable policy environment

Strengthening Institutional Mechanisms

1. Invest in investment facilitation infrastructure and expertise
2. Streamline approval processes were government route necessary
3. Strengthen dispute resolution mechanisms for investor grievances
4. Improve ease of doing business through digital platforms
5. Enhance capacity for beneficial ownership analysis

Sectoral Focus

1. Greater emphasis on high-technology sectors requiring significant capital and know-how
2. Promote sustainable industries aligned with climate goals
3. Encourage investments in manufacturing under Production Linked Incentive schemes
4. Focus on infrastructure development requiring long-term capital
5. Support innovation and R&D through foreign partnerships

Balancing Openness with Security

1. Regular review of FDI policy based on geopolitical developments

2. Sector-specific scrutiny mechanisms for sensitive technologies
3. Robust screening for dual-use technologies and critical infrastructure
4. Coordination with security agencies for risk assessment
5. Learning from international best practices on investment screening

Source - https -//www.thehindu.com/business/Economy/finance-ministry-notifies-fdi-easing-for-foreign-firms-with-up-to-10-chinese-stake-under-fema/article7093231