OPENING THE DOOR

Relevant for: Indian Economy | Topic: Issues relating to Growth & Development - Foreign Capital, Foreign Trade & BOP

On Wednesday, the NDA government announced a slew of measures aimed at **facilitating greater foreign investment** in the country. Under the new rules, it has provided for a relaxation of the contentious sourcing norms which have been a major deterrent for foreign investment in single-brand retail.

Now, firms can adjust their entire procurement from India, be it for their domestic operations or for global markets, against their local sourcing requirements. Further, local sourcing norms need not be met annually, but as an average of the first five years.

Sourcing, even through group companies or indirectly through third parties such as contract manufacturers, will now be counted towards their domestic sourcing obligations. Single brand retailers have also been allowed the option of setting up their online retail platforms before putting in place a brick and mortar presence.

Further, the government has allowed 100 per cent FDI in contract manufacturing and in coal mining and related activities such as washery, handling and separation. This easing of restrictions on foreign investment, which sends a positive signal to the international community, should be seen as a continuation of the measures announced by Finance Minister Nirmala Sitharaman last week to prop up the economy.

With the trade war between the US and China showing no signs of resolving, foreign companies are increasingly reassessing their operations. For instance, technology major Google is reportedly shifting the production of its Pixel smartphone out of China to Vietnam.

So far, India has not been able to take advantage of this ongoing relocation of production facilities out of China. But, these changes in the rules should gradually facilitate foreign firms setting up manufacturing bases in India, providing a boost to both employment and exports.

Allowing 100 per cent FDI in contract manufacturing through the automatic route will also attract global players looking to set up alternate manufacturing hubs — diversifying away from China. Adding exports to the local sourcing norms is also likely to encourage the building of larger production facilities, providing a much needed fillip to the country's subdued exports.

Sectors such as electronics, mobiles, apparel and pharma are likely to benefit the most from these measures. And with India's electronics imports exceeding $50 billion in 2018-19 — it was the biggest driver of the trade deficit after oil — over time, these measures could also help contain India's current account deficit.

These initiatives are an attempt to create a manufacturing ecosystem, establishing value chains with both upstream and downstream linkages. But they need to be accompanied by reforms, especially factor market reforms, that address the structural issues plaguing the economy.

The continuing overvaluation of the rupee also needs to be attended to. In the coming weeks, the government is likely to announce more measures to tackle the slowdown. These should be at the top of its agenda.

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