

Investment Strategy for India

Investment Commission Report

February 2006

Executive Summary

India has achieved impressive GDP growth of over 7% per annum in the last few years. However, sustaining growth at over 8% per annum will require a significant increase in investment levels in the economy - from approximately 30% of GDP to about 34% of GDP¹. Over the next 5 years, this translates to a cumulative investment of over \$ 1.5 trillion. The report undertakes to define a strategy that could enable India to achieve this investment goal. While expansion of domestic investment is essential to achieve this goal, FDI, which has been stagnant at about \$ 5 billion² in the past, also needs to be increased significantly - **the Investment Commission has set itself the goal to increase the level of FDI to \$ 15 billion by 2007-08.**

To this end, 25 key sectors spanning Infrastructure, Manufacturing, Services, Natural Resources and the Knowledge Economy have been studied. They represent a significant part of the economy, and between them would require an aggregate investment of \$ 525 – \$ 550 billion over the next 5 years. The sector studies also identified past investment levels, plans/ forecasts for future investment, as currently visible, and identification of the deterrents to investment.

Extensive investor interactions have provided key insights on policy and other impediments faced by investors. The Commission has interacted with industry bodies, associations, Ministries at the Centre and State level, business delegations and companies. Interactions also included meetings with business delegations from the US, UK, Italy, Japan and the Scandinavian countries with over 130 companies represented, altogether. Direct investor interactions (mostly personal meetings) were undertaken with an additional 64 international and domestic investors.

Arising out of these interactions, projects were identified for facilitation/ support totalling to a likely investment of about \$ 30 billion. Representations on policy/ procedures or other impediments were either resolved through reference to the Finance Ministry or have been incorporated in the recommendations in this report.

The major impediments to investment that span multiple sectors have been identified as:

¹ Assuming an Incremental Capital Output Ratio (ICOR) of 4.0; while this is higher than the current ICOR of ~3.6, it is based on the assumption that greater investment in infrastructure and manufacturing will increase ICOR going forward

² Less than 10% of China's FDI

1. Investment restrictions and/ or entry route barriers in several sectors of significant investment potential/ investor interest
2. Absence of long-term policies, non-implementation / reversal of policy and breach of contract
3. Lack of level playing field - especially in sectors with PSU dominance
4. Inflexible labour laws
5. Many agencies engaged in doing the same or similar activities relating to FDI
6. Bureaucratic delays, discretionary interpretation, vested interest, bias and subjective practices (In particular, approvals from Ministry of Environment & Forests seen as a major impediment in terms of inordinate delay).
7. Centre-State divergence on investment related policies
8. High cost of entry, transactions and exit; ineffective dispute resolution
9. Poor infrastructure
10. Priority Sectors are not clearly identified/ specified

Based on the investment goals and the identified impediments, a set of broad recommendations have been made which could facilitate and improve the investment climate. These are listed below:

1. Remove/ reduce restrictions on sector caps and entry route on all sectors other than those considered “strategic”. Permit “automatic route” for all investments within the sector cap.
2. Provide labour flexibility by removing the requirement of State Government approval from Chapter V-B and permitting Contract Labour in all areas
3. Promote SEZs for key sectors. Redefine norms on the basis of scale, investment quantum/ levels and sector focus. Separate the Developer of the SEZ from the Occupants
4. Provide a level playing field in sectors with PSU dominance - establish an Independent Central Regulatory Commission headed by a Chief Commissioner appointed by the President or the Prime Minister with independent Regulators for each regulated sector
5. Provide long term visibility and consistency of policy
6. Improve business environment – reduce number of procedures and approvals; make all approvals time bound and non-discretionary
7. Eliminate scope for discretionary interpretation to stem corruption – update key laws and statutes using Study Groups or Committees (with Government and Industry participation) to reflect this
8. Establish effective mechanisms to resolve centre-state issues – establish an

Empowered Committee framework (as done for VAT implementation) for implementation of key policies that require Centre-State cooperation such as Power sector reform, Labour law reform, Urban Land reforms (including ULC Act), APMC amendment

9. Other Recommendations

- Create a special high level fast track mechanism for priority sector projects
- Enhance availability of skilled manpower for sectors like Biotechnology, Automotive Engineering, Textile Engineering, IT – establish new private educational institutes with international collaborators
- Facilitate upgradation of Urban infrastructure by having a directly elected Mayor in key cities - as is the case with major cities in China and the USA.
- Establish a single point contact at the Centre to implement policies and procedures to enhance investment as well as facilitate high value projects across Ministries and Departments.

In addition, recommendations have also been made for specific sectors - Energy, Civil Aviation, Telecom, Metals and Mining, Textiles and Garments, Auto and Auto components, Food and Agro processing, Financial Services, Real Estate & Construction, Tourism and IT / ITES.

As the next phase of taking investment levels to a higher plane, the Investment Commission recommends:

1. The creation of National Thrust Areas – where the Government removes all impediments and provides special incentives for a pre-determined time period in order to achieve a specified growth. These could include Tourism, Power, Textiles and Agro-processing.
2. The hosting of Mega Events which will focus the country's attention on infrastructure development while also building national pride. Some ideas are: 2010 Commonwealth Games, 2020 Olympics, Football World Cup, Formula One Racing etc.

