# FOCUS WTO

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## INVESTMENT

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## From the Director's Desk

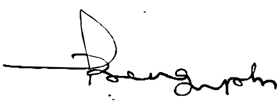
**Prabir Sengupta**

THE decision to initiate discussions on investment, particularly its relationship with trade, as one of the four "Singapore issues" after the first Ministerial Conference in 1996, was among the most controversial that the WTO has witnessed since its establishment. Most developing countries opposed any discussion on the possible linkages between trade and investment since they saw in this move an attempt by the developed countries to introduce in the WTO a multilateral agreement on investment (MAI), the framework of which was being discussed among the OECD Members. The overwhelming focus of the OECD MAI was on increasing the level of protection to foreign investors that had been granted by their host governments. But while their rights in the territories of their host governments were proposed to be increased, the obligations of the foreign investors were considerably diminished. However, despite the opposition from the developing countries to an inclusion of investment in the work programme of the WTO, a Working Group was established after the Singapore Ministerial Conference "to examine the relationship between trade and investment".

The developing countries, while accepting the view that a stable, transparent and predictable multilateral investment regime was essential for them to attract investment flows, argued that such a regime could not be ostensibly linked to the trading regime. Many of these countries argued that what was required was an investment regime that was consistent with the development priorities of the developing countries. This argument was made in much the same way as was done when the negotiations for a Code of Conduct for Multinational Corporations were under way under the auspices of the United Nations Centre on Transnational Corporations to examine the relationship between trade and investment. The Code negotiations brought home the point that a balanced framework had to be evolved, one which balances the interests of the foreign investors, on the one hand and the host countries, particularly from the developed world, on the other.

Since the collapse of the Code negotiations in the beginning of the 1990s, the tide has turned considerably towards the developed countries and their transnational corporations. This reality was reflected in the OECD MAI, wherein the proposed rights of the foreign investors were placed at a considerably higher pedestal.

The decision taken by the WTO members to drop investment from the current negotiating mandate of the WTO comes as an important development for the developing countries. These countries can feel somewhat at ease now that the deal that would eventually be struck at the end of this round of negotiations would not bring upon them onerous commitments in the realm of investment.



# Multilateral Framework on Investment

***Pradeep S. Mehta* and *Nitya Nanda****

## I. Introduction

DISCUSSION on a multilateral framework on investment (MFI) is by no means a new issue as it has been on the world-trade agenda since the aborted Havana Charter. Even during the Uruguay Round (UR) trade negotiations, developed countries advanced the idea of framing multilateral rules to further liberalize the foreign investment regime. But developing countries were opposed to any such idea. Eventually, the developing countries agreed to negotiate on four clusters of investment-related matters. The four sets of agreements under the auspices of GATT that relate to investment issues are: Trade-Related Investment Measures (TRIMs), General Agreement on Trade in Services (GATS), Trade-Related Intellectual Property Rights (TRIPs) and Agreement on Subsidies and Countervailing Measures (SCM).

TRIMs explicitly and exclusively deals with certain investment issues such as local content requirement, export commitment, dividend balancing, etc. The Agreement on TRIPs has a bearing on foreign direct investment (FDI) issue in which the definition of these rights and the adherence to international standards and procedures constitute part of the framework within which foreign investment takes place. The GATS also relates to FDI issue since it recognizes local presence as one of the modes of supply of service. With respect to SCM, certain investment incentives lie within the definition of a subsidy.

Besides, the Agreement on TRIMs has a built-in agenda under Article 9 of the agreement, wherein the Members can recommend expansion of the WTO acquis to both investment and competition policy. It was this provision that was invoked to bring on board the issues of investment and competition policy at the 1st Ministerial Conference of the WTO in Singapore in 1996. Further progress on this issue was made at the Doha Ministerial Conference as the Members agreed to decide on whether and upon what terms to launch negotiations at Cancun.

However, the Cancun Ministerial remained inconclusive with the issue of investment playing an important role in the collapse of the talks. After the Cancun fiasco, WTO discussions moved to Geneva. Following that, after about one year of expansive discussions, members of the WTO agreed on a framework of negotiations. As per the framework, three of the Singapore issues, including investment, have been dropped from the Doha round of negotiations. This, however, does not mean that the investment issue is shelved. Investment will continue to be an important area of discussions and will be brought to the certrestage of negotiations at the right time. The study process established through the Singapore declaration will most likely continue even after the issue of negotiations has been dropped.

One clear indication on this is available in the fact that investment policy features actively in various bilateral and regional trade agreements among the developing countries and in the discussions with the US and the EU.

## II. The Doha Mandate

The Doha Ministerial Declaration has the following three paragraphs on this issue:

***Para 20.*** Recognizing the case for a multilateral framework to secure transparent, stable and predictable conditions for long-term cross-border investment, particularly foreign direct investment, that will contribute to the expansion of trade, and the need for enhanced technical assistance and capacity-building in this area as referred to in paragraph 21, we agree that negotiations will take place after the Fifth Session of the Ministerial Conference on the basis of a decision to be taken, by explicit consensus, at that session on modalities of negotiations.

***Para 21.*** We recognize the needs of developing and least-developed countries (LDCs) for enhanced support for technical assistance and capacity building in

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this area, including policy analysis and development so that they may better evaluate the implications of closer multilateral cooperation for their development policies and objectives, and human and institutional development. To this end, we shall work in cooperation with other relevant inter-governmental organizations, including UNCTAD, and through appropriate regional and bilateral channels, to provide strengthened and adequately resourced assistance to respond to these needs.

***Para 22.*** In the period until the Fifth Session, further work in the Working Group on the Relationship Between Trade and Investment will focus on the clarification of: scope and definition; transparency; non-discrimination; modalities for pre-establishment commitments based on a GATS-type, positive list approach; development provisions; exceptions and balance-of-payments safeguards; consultation and the settlement of disputes between members. Any framework should reflect in a balanced manner the interests of home and host countries, and take due account of the development policies and objectives of host governments as well as their right to regulate in the public interest. The special development, trade and financial needs of developing and least-developed countries should be taken into account as an integral part of any framework, which should enable members to undertake obligations and commitments commensurate with their individual needs and circumstances. Due regard should be paid to other relevant WTO provisions. Account should be taken, as appropriate, of existing bilateral and regional arrangements on investment.

## III. Different Country Positions

The impression emerging from the WTO Working Group discussions pertaining to trade and investment indicates that most countries were (and are) still struggling to understand what are the contours of a possible multilateral framework on investment and its implications on their national development and industrial policies. Nevertheless, many developing countries were not so enthusiastic about the idea of launching WTO negotiations on an MFI. The most vocal opposition had come from the so-called like-minded group including India, Kenya, Malaysia, Tanzania, Uganda, Zambia and Zimbabwe among others. They were rather adamant about certain issues, which are crucial to them, thus posing a challenge for the future of the discussions. Some of the Latin American countries, on the other hand, have been quite sympathetic to the proposal, ostensibly because they believe that developing countries stand to gain from an investment agreement where they would collectively have more influence.

Unlike other countries, which seemed ambivalent, India and Malaysia have been steadfast in their opposition to an MFI at the WTO. According to India, investment is not a trade issue, therefore it does not belong to the WTO. It has also been argued that there is no evidence that an agreement will enhance investment flows into developing countries, hence, it would serve little purpose. Moreover, India and few other developing countries have consistently argued that Members must discuss the issue of mobility of labour (movement of natural persons) in any discussion on investment, as it too is a factor of production.

Pakistan has also repeatedly stated that it remains unconvinced of the need for an agreement adding that it would weaken the bargaining position of host countries *vis-a-vis* investors. The EU and Japan had tried to placate India and Malaysia as well as other developing countries by advocating an approach similar to that under the GATS. In their view, this approach would allow governments to open up areas where they want foreign investment and exclude those considered too sensitive for political, economic, or developmental reasons.

Most developing countries have also been in favour of including a narrowly defined and long-term foreign investment, i.e. FDI, in the possible MFI if there was to be one at all. The US too has never been an enthusiastic supporter of an MFI as it thought that the present approach of bilateralism is working quite well for it. However, it agreed to support the EU if the proposed framework was to its liking. The US has been asking for a high-satndard agreement, which would mean a broad-based and open-ended definition (which includes portfolio investment) and pre-establishment rights as necessary to maximize the benefits of investment liberalization and protection.

Australia suggested the idea of having a narrower definition for entry (pre-establishment treatment), and a broader definition for post-establishment treatment, in part for consistency with BITs. Canada supported an MFI as it felt that it can fill the gaps on WTO rules which only covers investment in services and not in goods. It argued that the concept of investor has to be sufficiently broad and should apply to the investor while in the process of investing (before and after the point in time at which the act takes place) as well as during the life of the investment.

Taiwan has been controversial by suggesting that Members should consider provisions for investor-state disputes through the dispute settlement system patterned after the Independent Entity Scheme for WTO Pre-shipment Inspection disputes. Most countries including Malaysia, Hungary, New Zealand, Hong Kong and China have objected to this proposal on the ground that it is beyond the Doha remit. The sentiment, however, is shared by most countries as they argue that the WTO was created for Members and not for private parties. Canada has suggested that a distinction should be drawn between agreements covering some investment provisions like GATS, TRIPs, and TRIMs and a new form of dispute settlement.

India made a submission, along with Cuba, China, Kenya, Pakistan and Zimbabwe spelling out investors' and home governments' obligations which includes preventing cases of corrupt corporate practices, fraud, and bankruptcies. These could also be used to protect the environment, bring transparency in the corporate world and control restrictive business practices, it has argued.

## IV. State of Play Around Cancun

According to the Doha Declaration, the Working Group on Trade and Investment was to work further on the clarification of the proposed elements, like scope and definition; transparency; non-discrimination; modalities for pre-establishment commitments based on a GATS-type, positive list approach, etc. However, these issues remain as complex as before to many of the developing country members and other stakeholders. The Declaration also spoke about possible modalities, consensus on which was essential to launch negotiation on the issue. But the issue of modalities were never discussed. The EU, Japan, Korea and Switzerland floated a draft note on modalities on investment agreement at the WTO just a few days before the Ministerial Conference.

However, the draft hardly went on beyond what had already been said in the Doha Declaration. Para 2 of the Draft said that paras 45 through 51 of the Doha Declaration would apply to the negotiations meaning that the negotiations on investment had to be concluded by 1 January 2005. Moreover, para 3 said that the negotiating group on investment would have its first meeting within a month of the decision, and the Chair would conduct negotiations with a view to presenting a draft text by 30 June 2004. This meant that negotiations and outcome would have been linked to the Doha Work Programme and would have been a part of single undertaking. This was quite undesirable as the negotiations on the Doha Work Programme started immediately after the Doha Ministerial, whereas the negotiations on investment were yet to begin. This was quite unrealistic even in absolute term as there would have barely been nine months to negotiate on such an important issue. Expectedly, some developing countries expressed their unwillingness for discussing the draft.

Wide divergence of views continued to emerge. This can be seen from the wording of the draft Ministerial Declaration that was circulated just before the Cancun Ministerial. For all the four Singapore issues, it envisaged two scenarios. In the *first* scenario, the Members agreed to commence negotiations on the basis of modalities set out in annexures. In the alternative scenario, the members recognized that the situation did not provide a basis for the commencement of negotiation in these areas. However, India and some other developing countries put forth their view of discussing those annexures adequately. Neither they had been circulated to the members. Interestingly, China also put its weight behind India on this issue.

Nevertheless, the EU and its allies continued to lobby to move ahead with all the Singapore issues including investment at Cancun. They even linked negotiations on investment with any possible concessions in agriculture. Predictably, there was stiff opposition from the developing world. Under such pressure, the EU agreed to drop investment along with competition policy, another Singapore issue. But it was probably too late. The talks at Cancun had collapsed.

## V. Conclusions

Among the four Singapore issues, investment has been the most controversial. Many developing countries are not convinced about its utility, as no evidence exists that an international investment agreement would increase investment flows to developing countries. Empirical studies have shown that FDI inflows are driven by several "gravity factors", like market size, income levels, availability of raw materials & labour, geographical & cultural proximity with major source countries and the quality of infrastructure. The policy factors that a multilateral agreement would try to regulate play a relatively minor role.

On the whole, the multilateral framework under the WTO includes many of the provisions that the exporters of capital from the developed countries have been demanding for long. Hence, developing countries anticipated that the post Uruguay Round era would significantly increase the flow of FDI, particularly to developing countries. However, investment flows to developing countries have not picked up so much as was expected. Share of developing countries in the global FDI inflow, however, increased once again in 2001, not because they performed better but the rich world was affected by the global slowdown in the aftermath of the September 11. This could be due to the fact that developing countries are already providing a reasonably stable investment environment.

Developing countries have never been very comfortable with the existing investment related provisions in the WTO acquis. The proposed agreement on investment, they fear, would further limit the scope for domestic control of transnational corporations without any balancing measures, particularly, in the context of LDCs whose economic might is much weaker than that of many TNCs. The agreement would tie the hands of governments trying to channel investment flows according to their national development strategies. There is also a concern that WTO rules might effectively give foreign investors preferential treatment over the national investors if the rules are modelled on the NAFTA investment provisions.

Developing countries point out that, initiatives were taken up by the United Nations to establish standards of behaviour for TNCs, particularly the Code of Conduct proposed by developing countries (the Group of 77). But, this effort was aborted in 1992 under pressure from developed countries, especially the US. Obviously, the proponents of an investment agreement have shown no inclination to include investors' behaviour or home country obligations in the proposed agreement.

Another issue that has always bypassed the discussions on international investment agreement is the issue of incentive race especially among the developing countries to attract more FDI. This is a process that might give advantage to some countries, but on the whole and collectively they lose. Obviously, this is a problem that cannot be tackled through bilateral initia-tives and poses a perfect case for a multilateral agreement. But this has not been on the WTO agenda.

It is noteworthy in this context that a multilateral agreement on investment (MAI) was attempted at the OECD. Discussions on the MAI faltered on the issue of rights to entry and establishment. In the negotiations, France clashed with the US over opening up its territory to the American audio-visual industry on the grounds that it would harm France's cultural and linguistic heritage. The negotiations proceeded in quite a tense manner and the issue died in 1999 when France pulled out after four years of negotiations.

It is quite strange that when the MAI could not be adopted by OECD members, who are relatively a more homogenous group, a similar - though a scaled down - agreement was attempted at the WTO where membership is much diverse. More importantly, it was done at the behest of the EU, in which France is a powerful member. It has been pointed out by many that the push for investment policy did not mean a genuine interest in an investment agreement but a Machiavellian game plan to stall any progress in liberalization in agriculture in which France has a strong interest. If that is indeed the case then probably the proposal for an agreement on investment at the WTO will be difficult to achieve as the July framework agreement already envisages substantial liberalization of agriculture. However, only future will tell how the July package moves forward!

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# NEWS (NATIONAL/INTERNATIONAL)

## Making A Case for FDI Hike in Telecom

THE Government intention to increase the foreign direct investment (FDI) cap from 49 to 74 per cent in the telecommunications sector is a timely reform business. Most countries have permissive FDI regime as opposed to restrictive regime and the choice of FDI regime has to be based on the country's own requirements which in India's case are our security concern and the need to attract greater investment.

While ownership has little correlation with vulnerability as security clearance for foreign partners and critical management by resident Indians could take care of any apprehensions on this score, the Finance Minister said neighbouring countries such as Sri Lanka, Bangladesh and Pakistan do not put any fetters on FDI in the telecom sector. Besides, the Tenth Five-Year Plan working group on telecom sector has estimated the investment requirement for this sector at a whopping Rs 1,60,000 crore.

The Finance Minister said that the growth in the telecom sector with mobile phones catching up all across the country regardless of the status of holders but serving them well in their small chores, "any slowing the growth momentum at this stage would lead to losing several direct and indirect benefits of the telecom growth".

The Finance Minister also mentioned that restrictions on mobile services even in developed countries are more due to spectrum availability rather than any ideological or security considerations. He reeled out the rewards of increasing liberalization in this sector with FDI resulting in better spurs for technology transfer, improved management and in lower prices for users.

More recently, the World Trade Organization (WTO) in its 2004 *World Trade Report* analyzing the theme "Exploring the linkage between the domestic policy environment and international trade" elegantly captured how effective telecommunications provide a low-cost channel for searching, gathering and exchanging information which is a key input in all economic activities.

For many industries, the telephone is the primary point of selling and the Internet is an increasingly important mode of communication for some industries with e-commerce and electronic data interchange (EDI) for foreign trade operations coming in a big way in India.

WTO said that it is now possible for countries that have lagged in economic and technological development to switch over to the most recent technologies at relatively low costs of adoption.

A particularly noteworthy aspect but which many in their myopia miss is that the digital divide is narrower and narrowing faster than the income gap between rich and poor countries, the WTO said adding that while GDP per capita grew at almost the same pace in low income and high income countries during the period 1995-2001, the number of mobile phones per 100 inhabitants grew almost twice as fast in low income countries.

Available trends in India too suggest that mobile users are going to outnumber fixed-line users before long, presaging the tangible benefits this confers on a large number of people.

WTO says that an analysis of the relation between service supply and the extent to which foreign entry is restricted finds that the more restricted is foreign entry, the lower the mobile telephone density. "It is also worth noting that the more open market-based mobile services have provided a narrower international digital gap than the state-controlled fixed-line services," WTO said.

It is time that opponents to hike in FDI cap in telecom sector recognize these simple but valid points so that the Indian economy is not condemned to remain mired in high-cost mode in perpetuity, say policy analysts.

(*The Hindu Business Line*, 15 October 2004)

## India Jumps to No. 3 in FDI Confidence Index

INDIA has climbed three notches to grab the number three position on AT Kearney's FDI confidence index for 2004. This is India's highest ranking ever. India rose from sixth to third most likely FDI location globally, just behind USA. It displaced Mexico which has dropped to the 22nd place.

China has maintained its top ranking as the most attractive FDI destination. Although USA has remained the second most attractive FDI location the gap between USA and India may be closing, according to the latest annual survey of executives from the world's largest companies, conducted by the global management consulting firm. Among manufacturing investors, for the first time in the index, India displaced USA to become the second most attractive FDI location.

China and India dominate the top two positions for most positive investor outlook, likely first-time investments and most preferred offshore investment locations for business processing functions and IT services. Global executives are more likely to invest in China and India now, than at any time since '98 and corporate investors have expressed increased keenness for overseas investments compared to '03 – the first positive year-to-year increase in overall FDI confidence since 2001.

However, global investors view these two destinations as distinctly different markets: China – world's leading manufacturer and fastest growing consumer market and India – world's business process and IT services provider with longer-term market potential. Compared to other large emerging markets, China and India were cited by the surveyed CEOs as the most attractive FDI destinations in the short-term (next three years) and well into the future, beating markets like Brazil, Mexico and Poland for medium-term attractiveness 10 years out.

Investors favour China over India for its market size, access to export markets, government incentives, favourable cost structure, infrastructure and macro-economic climate. These investors cite India's highly-educated workforce, management talent, rule of law, transparency, cultural affinity, and regulatory environment as more favourable than China. China's FDI flows are larger ($53.5 billion) and primarily capital-intensive, while Indian FDI flows are smaller ($4.3 billion) and skill-intensive.

CEOs also expressed highest optimism levels in years. Nearly 70 per cent of global investors are more upbeat on the global economy this year. The last time a majority of investors were so bullish on the global economy was in 2000, when global FDI flows reached the all-time high of $1.4 trillion. For the first time since '01, surveyed executives' overall willingness to invest overseas rose.

India displaced Mexico to become the third most attractive FDI destination worldwide and is increasingly perceived as an R&D hub for a wide range of industries. The country's service-oriented development path is allowing it to bypass obstacles like weak infrastructure. A "wired" India has played to its strengths, which include a well-educated, IT-savvy workforce with English-language proficiency. Yet, according to global investors, bureaucracy, political stability and maintaining a lower-cost advantage will be the principal challenges to India's future competitiveness.

(*The Economic Times*, 13 October 2004)

## India Up Three Notches in FDI Index

INDIA is speeding ahead and may soon overtake USA as the second most favoured destination for foreign direct investment (FDI). It has already overtaken Germany, Poland and Mexico by moving up three notches to third rank in AT Kearney's FDI Confidence Index 2004.

China still leads the race and has maintained its *numero uno* position, followed by USA. The UK too has improved its position by three slots and follows India as the fourth most attractive destination.

The latest FDI Confidence Index (an annual survey of executives from the world's largest companies) conducted by management consulting firm AT Kearney, released in London, says the gap between USA and India may be closing as both China and India, though competitive between themselves, are giving a tough fight to USA as an attractive FDI destination.

In fact, for the first time in the Index, India has displaced USA to become the second most favoured FDI location among manufacturing investors. "Never before has USA been ranked so low among manufacturing investors," says the report. The executives said India's strong performance among manufacturing, telecom and utility firms was largely due to the country's "desire to make productivity-enhancing investments" in IT, BPO, R&D and knowledge management activities.

The CEOs said they were more likely to invest in evolving economies like China and India than at any time since 1998. However, they viewed both the countries as "different" markets — China, as a manufacturing hub and growing consumer market and India, as the world's leading business process and IT service provider.

On offshoring activities, the CEOs predictably indicated manufacturing and assembly as the two focus areas in China; and IT, business processing and R&D in India.

This is the third year in a row that USA is lagging China as a favoured FDI destination. This time the spread is across all major sectors — financial and non-financial services, manufacturing, primary, telecom, utilities, and wholesale & retail.

Overall, nearly 70 per cent of the CEOs were upbeat on the global economy. This renewed confidence may lead to higher overseas investments, said the report. However, there were some areas of concern. In all 51 per cent of the respondents viewed currency and interest rate volatility as critical risks to their operations compared to 63 per cent last year. Surprisingly, the oft-cited government regulation and macroeconomic, political and social instability seemed to be slightly less daunting for investors this year.

(*The Financial Express*, 13 October 2004)

## Kamal Nath Makes Case for Job-Generating FDI

THE Government welcomes FDI, but investments for mere acquisitions do not excite it. Investment in trading operations would, however, be viewed rather positively, as it leads to economic activity. This was stated by Commerce and Industry Minister Shri Kamal Nath in his address at a luncheon meeting "Celebrating Indian Investment in the UK" in London.

"Foreign investors would find a very conducive atmosphere in India. While all kinds of FDI is always welcome, our very comfortable foreign exchange reserves means that investment for mere acquisitions do not excite us. What we really want is FDI that generates the maximum economic activity, and thereby generates employment, that creates wealth for our people," the Minister said. "Employment generation was a central election promise of ours. We especially therefore look to FDI in manufacturing sectors and in greenfield projects".

The age of the Indian MNC has now dawned, with the Indian industry realizing that worldwide, businesses can thrive today only by crossing new frontiers, creating new markets and building new partnerships, he said.

The very theme of the gathering symbolized the transformation of the UK-India commercial links over the years and the new economic paradigm of two-way investments, which was emerging, he said.

Pointing out that India's two-way international trade stands at $150 billion and foreign exchange reserves of the country are a comfortable $120 billion, Shri Nath indicated that "the value of overseas acquisitions by Indian firms leap-frogged in the first half of 2004, with 24 buyoffs valued at a billion dollars, or roughly double the size of all of last year's acquisitions."

Indian companies are investing heavily in different parts of the world, including Germany, the United States, Australia, China, Korea, Thailand, Singapore and many parts of Africa.

(*The Economic Times*, 12 October 2004)

## India's FTAs to Offer FDI Hopefuls A Breather No Matter Which Way Draft Proposal Goes

A section of industry feels India's free trade agreements (FTAs) with Thailand and other countries in the ASEAN, Latin America and Africa will offer multinational FDI hopefuls a breather, no matter which way the draft proposal on the modified Press Note 18 goes.

Thanks to the FTA regime, it will be possible for companies to source from neighbouring markets like Thailand where, in industries such as automobiles, the MNC footprint is fairly strong. Indeed a number of MNCs have a strong presence in many of these markets that are among the biggest volume markets among emerging economies.

A section of industry feels India's FTA push may dilute the negotiating muscle that the Press Note 18 arms local partners with, in a joint venture with a multinational company.

And that irrespective of whether the draft proposal for the modified Press Note 18 includes a sunset clause or not, once the ASEAN free trade agreements kick in by 2010, the no-objection certificate (NOC) will no longer be an issue for local manufacturing. The sunset clause has been the most contentious part of the Press Note 18 and industry has been divided over its potential inclusion in the modified draft.

However, the distribution-only structure may not be valid for companies looking at volumes and a large presence. Because an Indian entity, which can be blocked in the absence of an NOC from a former JV partner, is necessary for a whole host of activities, even if manufacturing is excluded.

While the manufacturing alternative is now open post-FTA, there are other reasons why MNCs need to set up subsidiaries in the country. While a distribution arrangement is alright if the scale of operations and volumes is small, as is followed by some businesses, it can seldom work on a much bigger scale.

Often MNCs enter a country by setting up distributors to check out the market. Later on when they are sure that they want a presence in the country, they set up a subsidiary or a joint venture. In case they don't want full-scale presence, they sell technology through a technical collaboration agreement. There are many MNCs that have subsidiaries here without having any manufacturing base. In these cases, the function primarily remains restricted to sales and marketing.

(*The Economic Times*, 9 October 2004)

## Plan Panel Wants Auto, Pharma Off Press Note 18

THE Planning Commission has suggested that sectors such as food processing, automobile and pharmaceuticals should be exempted from the purview of Press Note 18 for incorporation of new joint ventures through the automatic route, if the government were to decide against scrapping the regulation.

The Commission also said that joint ventures (JVs) being incorporated in the north-east and eastern regions be exempted from the requirements of the Press Note 18.

Another suggestion of the Commission is to allow the foreign partner in a JV to sell its stake in an existing JV either to its partner or to a domestic company before incorporating a new entity in the same business area or allied activity — as a JV or a wholly-owned subsidiary — in the country.

Sources said that the Planning Commission favoured outright scrapping of the Note as it felt that the regulation had outlived its utility, and the environment in which it was introduced had undergone a sea change.

The Commission — which has been directed to prepare a note on the future of the Press Note by the Cabinet Secretariat for consideration of the Committee of Secretaries — felt that a complete withdrawal of the Note would enable the creation of a competitive environment conducive for growth.

Mining companies, for instance, are allowed to incorporate 100% subsidiaries and use the automatic route for approval if they do not have an existing JV in the same area or mineral.

Similarly, multilateral agencies such as ADB, IFC, CDC and DEG are exempted from seeking Foreign Investment Promotion Board (FIPB) approval for acquiring stake in companies in the same sector, provided the investment was within the overall foreign investment cap for the sector.

The Commission felt that the three sectors — food processing, automobiles and pharmaceuticals — had the potential to attract large amounts of foreign investment and, therefore, like IT and mining, should be out of the purview of the regulation.

(*The Economic Times*, 9 October 2004)

## India is Second Most Attractive Retail Destination: AT Kearney

AT KEARNEY has ranked India as the second most attractive retail destination among emerging markets globally, ahead of China, despite the ban on Foreign Direct Investment (FDI) in the sector and a relatively low market attractiveness of the country.

In its 2004 "Global Retail Development Index (Top 30 Emerging Markets)" report, AT Kearney has ranked India 88 on a scale of 100, aggregating points earned over parameters such as economic and political risks, market attractiveness, market saturation and time pressure. Russia, with 100 points, is the most attractive emerging retail destination, says the report.

The report suggested India's market size offered "tremendous promise as its population is expected to surpass China's by 2050. India's country risk score (62) is higher due to improved living standards and continuing economic growth". Even dampeners such as stringent FDI rules have failed to move India from its vantage point in the list.

"India's market attractiveness score is relatively low (34) because of its large rural population but it earns marks in other areas. Retail sales per capita have increased by one-third between 1999 and 2003," it said. Other downsides include a fragmented retail market with the top 10 companies holding only about 2 per cent of the market share.

The report said two foreign retailers - Hong Kong-based Dairy Farm and Metro AG - are in the top five; and South African retailer Shoprite is also considering of making a foray into the country.

Besides, a number of companies, including Wal Mart and Carrefour, have expressed interest in India if FDI regulations are eased, since at present foreign ownership of local retailers is not permitted. "Until reforms pass, successful global retailers will have to adapt and enter using different formats. For example, for the past two years Planet Sports India has operated two franchise stores for Marks and Spencer," the report pointed out.

India is closely followed by China with a total score of 86. AT Kearney said that though China was also an attractive retail destination, economic and retail indications are showing "signs of stagnation".

In its overall assessment of the global retailing scenario, AT Kearney said 2004 represents a revival of mass merchants and food retailers and that this year, discounters have entered the fray "significantly changing the competitive landscape in emerging markets where consumers are more price conscious".

The annual AT Kearney Global Retail Development Index ranks 30 emerging countries on a 100-point scale - the higher the ranking, the more urgency to enter a country. The 30 countries were presented from a list of 185 based on criteria including a country risk score of more than 40, population of over two million and GDP per capita over $2,000.

(*The Hindu Business Line*, 6 October 2004)

## Korea All Out to Boost Trade

INDIA and Korea are exploring a comprehensive economic partnership in a bid to bolster trade and investment flows between the two countries.

This could well include a free trade agreement (FTA). The Commerce & Industry Minister Shri Kamal Nath has said that India and Korea should aim for a relatively evenly balanced total annual trade of $10 billion within three years and a sustained average FDI of $1 billion.

"These are not impossible targets... I know we can achieve it if we go about our tasks with single-minded determination", he said while addressing the business meeting organized by the Confederation of Indian Industry (CII) and the Federation of Indian Chambers of Commerce and Industry (FICCI) on the occasion of the state visit of Mr Roh Moo-Hyun, President of Republic of Korea.

Referring to the proposed comprehensive economic partnership between India and Korea, Shri Nath suggested that the group which would discuss the framework of the economic partnership should go about its work in a target oriented manner by first defining the target and the time-frame and then working out the best way to achieve the annual trade and FDI targets.

Total trade between India and Korea last year stood at around $3.3 billion. India's exports were $800 million, whereas imports from Korea were $2.5

billion. India's exports to Korea comprise a high proportion of primary products like agri products and dyes and pharmaceuticals whereas the major items of India's imports from Korea are industrial goods like electronics, machinery and transport equipment. There is ample scope to diversify the trade baskets.

As regards investment, although Korea was the seventh largest FDI investor in India, cumulative FDI inflow from Korea during the last 13 years was only about 3 per cent of India's total inflows and it did not account for even $1 billion.

However, the recent announcement by Korean steel major Posco to make huge investments in Orissa would itself transform the FDI figures dramatically.

(*The Economic Times*, 6 October 2004)

## 5% Cap Only for Foreign Banks Already Present in India

### RBI May Ease 10% FDI Cap for Non-Banking Entities

THE final Reserve Bank of India (RBI) draft on ownership and governance in private banks may ease Foreign Direct Investment (FDI) by a single non-banking entity beyond the currently proposed 10 per cent.

RBI is also set to clarify its position on the thorny issue of foreign bank holdings in Indian private sector banks.

In its view, the proposed 5 per cent cap on foreign bank holdings in private banks covers only those foreign banks which have existing operations in India. Therefore, this 5 per cent is being viewed as a "financial investment". For foreign banks, which do not have a presence in India, a separate set of norms is being readied which will facilitate bank acquisitions.

These guidelines would deal primarily with private banks, a separate set of guidelines will be issued later on foreign bank holdings in India.

In the first draft on the new private bank norms, RBI had proposed to cap FDI by a single entity or a group of related entities at 10 per cent, within the overall 74 per cent foreign holding limit.

However, sources said the central bank may, in some cases, want to allow entities to go beyond that limit if these entities seek prior approval and discuss these issues with RBI. "This window has to be left open in the final norms," sources said. This will also be in accordance with RBI's February 2004 guidelines for acknowledgment of transfer/allotment of shares in private sector banks.

A critical aspect of FDI in this case is that it does not pertain to foreign banking entities. This 10 per cent limit only pertains to non-banking entities like private equity funds and others.

RBI's thinking on the issue of foreign banks is clear. The central bank says the guiding principle is the concept of "single presence". This means a foreign bank can be present in India in only one form: either as a branch or a subsidiary. If an existing foreign bank holds a stake in another Indian private bank, then it will fall under the category of "financial investment", for which the cap is the proposed 5 per cent.

(*The Financial Express*, 6 October 2004)

## Agreement between Indian, Foreign Partner is the Last Word: Modified Note 18 to Cut Back Veto Power, Govt Discretion

A DRAFT proposal prepared by the Government to modify Press Note 18 substantially dilutes the veto power currently enjoyed by the Indian partner in a joint venture with a foreign major. At present, the Indian partner has the power to veto any associated business floated exclusively by the foreign partner. This is valid even after they have long parted ways. In its current avatar, the Press Note 18 gives this power to the Indian company on any new venture as long as it is "in the same line of business."

However, the new policy may move that discretion away from the government and leave the entire matter to an agreement between the two partners. After this, government policy, including Press Note 18, cannot override the shareholders' agreement. This will virtually render the most contentious aspect of the Note redundant.

Normally, the Press Note 18 diktat is enforeceable within a "time-bound" period of two years after the expiry of the licence. The current feeling among a section of industry is to modify Press Note 18 to prevent unjustified blocking of new investments by the foreign partner in a 100% owned subsidiary.

Among the options being thrown up is a review committee on NOC spats and a cooling off period in related businesses.

In the automobile business, for instance, there are cases of the Indian partner being able to negotiate a sunshine deal to buy out the foreign partner on the basis of a no objection certificate (NOC) being offered upfront. However, in other industries where the going has been very tough for the domestic company, the foreign partner has been buying them out at a premium, once again based on the NOC clause.

In the new scenario, much of this will become unnecessary as the importance of the NOC will dwindle. The shareholder agreement will decide expiry of a partnership as well as the fate of a 100% subsidiary.

(*The Economic Times*, 6 October 2004)

## FDI, FII Distinction to be Kept

THE Finance Ministry is likely to retain the distinction between Foreign Institutional Investors (FII) and Foreign Direct Investment (FDI) in the banking sector. In the telecom sector, however, FII and FDI can be clubbed in determining the overall foreign investment cap.

According to the Finance Ministry, it is necessary in the banking sector to differentiate between mere investors and those who want management control. “Here, one needs to know who owns the enterprise, whether it is FDI or FII. We need to know if he is coming as an investor or is asking for management participation,” an official said.

Fungibility of FDI and FII, perhaps, makes sense in the telecom sector. “Everybody wants to come mainly as an investor, for the purpose of growth and income,” the official said. The present guidelines allow 49 per cent FDI inclusive of FII holding. It has been proposed to raise this ceiling to 74 per cent in the current Budget.

In private banks, the present guidelines allow 74 per cent FDI, again inclusive of FII holding. The Government is now planning to let foreign banks make a gradual entry into India by allowing them creeping acquisition of, say 10 per cent a year, for the next 3-4 years. During this period, Indian banks can consolidate and prepare themselves for a stricter regulatory regime.

The committee on liberalization of FII under Chief Economic Advisor Ashok Lahiri, has recommended 100% foreign investment in private banks. It has, however, not prescribed any sub-ceilings for FDI and FII. The committee has made an exception for four sectors: telecom, public sector banks, defence production and insurance, while recommending in general that FII investment should come over and above the FDI caps.

In telecom, it has recommended a composite 74 per cent cap without sub-ceilings on FDI and FII. In defence production, it has said the present 26 per cent FDI cap can be raised to 49 per cent FDI-plus-FII cap. Similarly, in insurance, it recommended raising the overall foreign investment cap from 26 per cent to 49 per cent.

For public sector banks, where there is currently a statutory 20 per cent composite cap on foreign investment, the committtee has recommended additional 20 per cent foreign institutional investment. Respective Acts can be amended to raise the cap to 40 per cent. It has, however, said FIIs should not have any board representation in public sector banks.

(*The Financial Express*, 4 October 2004)

## Scrapping Press Note No. 18 will be Myopic

A section of India Inc — in particular, that which has been running successful joint ventures with foreign partners — is perturbed over the Government’s concerted move to scrap Press Note No. 18 in its bid to usher in larger inflows of FDI.

Scrapping the provisions of the “domestic investor-friendly” circular would be an extremely myopic decision as it would do more harm than good to the country’s manufacturing sector. For, the larger dose of FDI, if at all, could well be at the expense of the numerous currently thriving joint venture operations, they say.

And, to drive home their view, they point to the recent skirmish that the Indian Government had with Suzuki Motor Corporation of Japan, its majority foreign partner in Maruti Udyog Ltd. In the hurried negotiations, what saved the day for the Government as the Indian partner in the joint venture were the provisions of Press Note No. 18, they point out.

Essentially, the Press Note, which has been a stumbling block for some foreign investors, stipulates that if any foreign investor, who has a running joint venture with an Indian partner and wishes to set up its wholly owned subsidiary in the country in the same line of business, he will have to seek the prior permission of the domestic partner. For this, the prospective foreign investor will have to furnish a "no objection certificate" (NOC) from the Indian partner to enable the authorities to process the fresh investment proposal. In effect, in the absence of the NOC, the new investment proposal will stand rejected.

To cite specific instances, Walt Disney's plans for setting up a wholly owned subsidiary had initially faced rough weather following objection by the Modi group, the joint venture partner of Walt Disney India Pvt. Ltd. Similarly, Haier's plans for a wholly owned subsidiary were stalled owing to the Baron group standing in the way.

Thus, this uncompromising stipulation as far as the interests of the foreign investor are concerned, is being viewed, of late, as one of the major factors inhibiting large doses of fresh investment inflow. And the Government eager to being seen as instrumental in luring larger inflows of FDI, the matter has been taken up by the Finance Ministry.

Industry watchers, however, warn that such a move would immensely benefit the foreign investor but only at the expense of the existing domestic partners. For, once the foreign partner is allowed to set up a wholly owned subsidiary, he would "prefer to have the whole pie rather than share the booty with a domestic partner." In effect, there would be chances that some of the highly successful joint ventures, especially in the auto sector, may face a period of turmoil, these sources point out.

(*The Hindu Business Line*, 4 October 2004)

## India Dons Foreign Direct Investor Mantle

BUOYED by the inroads made by its software, biotech, auto ancillary and oil companies abroad, India seems to have dropped the tag of being just an FDI destination and is increasingly donning the mantle of a major foreign direct investor. And the investments span not only across the developing world but even in first-world nations including the US, the UK and Germany.

With annual outflows averaging at $1 billion (around Rs 4,600 crore), the country's ranking in UNCTAD's outward FDI performance index has already shot up from the 107th position in 1999 to the 61st spot in 2003.

Even more noteworthy is the fact that the two most important destinations for Indian FDI last year were the US and the Russian Federation, accounting for around 37 per cent of the total Indian overseas investments during last year, while Europe accounted for 40 per cent of the total outflow.

The top 15 software and service companies in the country have all invested abroad, while Indian BPO firms are setting up outfits in countries as varied as Mexico and the Philippines.

ONGC's 25 per cent stake buy-out in a Sudan oil firm from Talisman Energy of Canada for $720 million (around Rs 3,312 crore), the Hinduja's purchase of controlling interest in C3, a call centre in the Philippines, and Msource's Spanish language centre in Tijuanna, Mexico, were among the large investments by Indian firms abroad last year, according to the UNCTAD data.

Bharat Forge's acquisition of CDP in Germany, Amtek Auto's acquisition of GWK in the UK, and Sundram Fasteners' acquisition of Cramlington Precision Forge Ltd marked the Indian auto ancillary companies' foray into the global market.

According to analysts, the UK remains the gateway for investments by India Inc in Europe.

During 2003-04, the country has seen a 47 per cent jump in investments, as compared with the previous year. According to a report by the UK Trade and Investment, India is now the second largest source of FDI into the UK from Asia in terms of projects and jobs generated, while it ranks eighth overall.

The emergence of India as a major force in the investment scenario seems to have prompted visits by delegations from the UK and the Invest in France Agency (IFA) to try and woo Indian industry bigwigs to invest in their countries.

The first six months of the current fiscal has seen a significant increase in FDI outflow, with companies such as Tata Steel, Reliance, Raymond, Jubilant Organosys and Jindal Stainless emerging as corporate raiders overseas.

(*The Hindu Business Line*, 1 October 2004)

## 26% Divestment Clause for Foreign Companies May be Dispensed With

THE government is formulating a policy that will exempt foreign companies from the mandatory disinvestment of 26 per cent equity to the public.

Allowing German pharma major Fresenius Kabi India to dispense with the mandatory 26 per cent disinvestment clause, the Government has noted that “a consistent view needs to be taken in all such cases where a liberalized policy dispensation is available”.

“The matter has been taken up with the Department of Industrial Policy & Promotion (DIPP), which is concerned with FDI policy,” a government source said.

While exempting Fresenius Kabi India from divesting equity, the Foreign Investment Promotion Board (FIPB) cited the case of JP Morgan Securities. Waiving the disinvestment clause in the JP Morgan case, the Board last year observed that a liberalized policy should be formulated in sectors where 100 per cent FDI is allowed.

Fresenius Kabi’s case comes close on the heels of global oil majors - Caltex, Shell, Exxon-Mobil, Total Petroleum and ELF - which were allowed to dispense with the mandatory 26 per cent disinvestment clause. These companies were exempted from divesting twenty-six per cent equity in their wholly-owned Indian subsidiaries in the light of changed FDI guidelines, which allow 100 per cent foreign equity in trading of petroleum products.

The Indian subsidiary of the 1.5 billion euro major had sought deletion of the divestment condition earlier, but it was withdrawn from the FIPB agenda pending a policy decision. The Government took up the case again after allowing 100 per cent FDI in the chemical and pharmaceutical sector.

The company said in its application that it established its plant at Pune with the help of the parent, which provided state-of-the-art technology without any royalty payment. Further, changing the ownership structure without any business reason would be “detrimental to the production of world class products”.

The company also stated that sharing of R&D depends on protection of intellectual property rights. Changing ownership would also result in cancellation of existing manufacturing licences and WHO approvals, the company stated, and it would have to obtain fresh licences.

(*The Financial Express*, 1 October 2004)

## Press Note 18 May be on Its Last Legs

THE controversial Press Note 18, which requires foreign companies to compulsorily obtain a no objection certificate (NOC) from their existing Indian partner before setting up a new venture in a similar line of business, may be dumped.

Finance Minister P. Chidambaram said, “The utility of Press Note 18 may be over.” He said that there was a strong case for reviewing the utility and continued relevance of Press Note 18.

According to Finance Ministry, any decision on Press Note 18 will need to be taken only by the Union Cabinet. They said apex industry associations including Confederation of Indian Industry (CII) and Federation of Indian Chambers of Commerce (FICCI) were against withdrawal of the notification.

CII is of the view that genuine grievances of foreign investors may be discussed. “Press Note 18 may be modified, but should not be scrapped as it serves a useful purpose,” CII Director General N. Srinivasan said.

The notification has been invoked by several Indian companies in the past to block their foreign partners from setting up a new venture in a similar line of business through a 100 per cent subsidiary.

The Foreign Investment Promotion Board (FIPB), till 2002, had generally seen merit in the Indian partners' contention.

Over the last two years though, FIPB has been taking a more liberal view on such objections raised by defunct Indian joint ventures. For instance, in cases like Graphite-Widia India Ltd and Baron-TCL, the Board ruled in favour of the foreign company.

The officials said that in a liberalized environment, Press Note 18 placed several restrictions on foreign investors and in a way discouraged FDI into the country. While the Ministry was likely to do away with the need to approach FIPB for routine clearances like transfer of NRI stake, etc, no final view has been taken on Press Note 18.

(*The Financial Express*, 30 September 2004)

## Automatic Route Window Widens

THE Government has announced the simplification of foreign investment procedures by putting three more categories under the automatic route: a hike in foreign equity in a company, transforming preference shares into equity capital and conversion of foreign loans taken by a company into equity. Of course, there is a caveat: there should not be a breach of the sectoral foreign investment caps.

In addition, the Finance Ministry also allowed the transfer of shares from resident to non-resident (including transfer of subscribers' shares to non-resident) other than in the financial services sector under the Reserve Bank of India's (RBI) general permission route.

The measures are part of the Government's efforts to make India a more attractive destination for foreign investors and speed up and streamline investment approvals, according to a release.

The release said, there would be no need to obtain clearance from the FIPB. Instead they were put under the automatic route (general permission) under the RBI.

According to the release, the automatic route in the case of transfer of shares from resident to non-resident would be subject to compliance with the provisions of the Securities and Exchange Board of India relating to the Substantial Acquisition of Shares and Takeovers Regulation of 1997.

RBI clearance would also be applicable if the transfer of shares fell within the sectoral cap and also complied with the prescribed pricing guidelines.

Similarly, the conversion of external commercial borrowings and loans into equity can also be cleared by the RBI, provided the activity of the company was covered under the automatic route.

The level of foreign equity after such conversion should fall within the sectoral foreign investment limit and the prescribed pricing guidelines.

The onus of complying with the sectoral caps or limits prescribed under the FDI policy as well as other guidelines or regulations would rest with the buyer and seller or issuer, the release said. It added that the necessary notifications and circulars under the Foreign Exchange Management Act would be brought out by the RBI.

(*Business Standard*, 30 September 2004)

## UNCTAD Report Optimistic on Global FDI Inflows This Year

THE United Nations Conference on Trade and Development (UNCTAD) said that though global inflows of FDI fell in 2003 for the third year in a row to $560 billion, prospects for the current year are promising.

In its 2004 *World Investment Report*, released by the Director-General, Research & Information System (RIS) for Non-Aligned and Other Developing Countries, Dr. Nagesh Kumar, the Geneva-based UN body premised its optimism on cross-border mergers and acquisitions (M&As), which though still low at $297 billion in 2003, have begun to pick up. They rose by three per cent in the first six months of 2004 over the same period in 2003.

This coupled with other factors such as higher economic growth in the main home and host countries, improved corporate profitability and higher stock valuations, points to a recovery of FDI flows in 2004.

Reflecting higher profits, reinvested earnings - one of the three components of FDI - are also expected to pick up in 2004.

Corroborating this optimistic picture are surveys conducted by UNCTAD during the first quarter of

2004 of 335 of the world's largest transnational corporations (TNCs) and 87 global site-selection experts.

These reveal that flows are likely to pick up, particularly in Asia and the Pacific and in Central and Eastern Europe (CEE) countries. China and India in Asia, and Poland in CEE are considered to be especially well-positioned for an upswing.

India's FDI inflows amounted to $4,269 million in 2003, against $3,449 million in 2002, while FDI outflows amounted to $913 million, against $1,107 million in 2002. It ranked 114 in an inward FDI performance index and 61 in outward FDI performance.

India's services sector, in particular information and communication technology (ICT) industries, was the most dynamic for inflows.

The UNCTAD investment report is bitter about flows to India getting increased with the Government having announced the objective to raise FDI flows by two to three times.

The agreement among South Asian countries to establish the South Asia Free Trade Area and the improved geopolitical situation must strengthen the investment environment, it said.

Prospects are bright for some services and for electrical and electronic equipment, motor vehicles and machinery.

Greenfield investment is predicted to dominate FDI in developing countries and cross-border M&As in the developed world.

In 2003, 86 bilateral investment treaties and 60 double taxation treaties were concluded, bringing the total to 2,265 and 2,316, respectively.

The inward FDI performance index shows that economies such as the Czech Republic, Hong Kong and Ireland continued to attract significant investment even during FDI recession.

In contrast, countries such as Japan, South Africa and Thailand have yet to realize their full potential to attract FDI.

While TNCs from developed countries would drive the renewed growth of world FDI flows, the share of TNCs from developing countries also rose from less than six per cent in the mid-'80s to 11 per cent during the latter half of the '90s, before falling to seven per cent in 2001-03 (for an annual average of $46 billion).

(*The Hindu Business Line*, 23 September 2004)

## India's Potential to Draw FDI Low, Says UNCTAD

RANKED 114 in the inward foreign direct investment performance index for 2001-03, India not only has a low potential of attracting foreign direct investment (FDI) but also is an under-performer in this respect, according to UNCTAD's *World Investment Report 2004* (WIR '04).

India has been clubbed with the likes of Indonesia, Argentina, Bangladesh, Pakistan and a host of African countries as an "under performer" on the basis of performance and potential. China, Bahamas, Belgium & Luxembourg, the UK and Canada have been termed as the front-runners, while the US, Australia, Japan, South Africa and South Korea are classified below potential.

In the listing based on performance, Belgium & Luxembourg is at the top of the list, with China placed 37th, Pakistan at 97, the US at 112, which is two notches higher than India.

In the potential rankings, India does not figure in the top 25 list with the US leading the charts followed by Norway and the UK.

The *WIR '04*, however, has termed India as having a promising future as a large outward investor, recording $1 billion of annual outflows during 2001-03. The latest outward FDI performance index for 2001-03 shows that India has climbed up two ranks to 63 from 61 during 2000-02.

India was, however, placed among the top four Asian FDI destinations and said it would get more foreign investment flows as global economy rebounds this year.

The foreign direct investment performance index is the ratio of a country's share in global FDI outflow or inflow to its share in global Gross Domestic Product.

An inward index greater than 1 indicates that the country attracts more FDI in proportion to its economic size.

The *WIR '04* points towards a shift, where developed countries suffered a relative decline in positions in the inward performance index, while the "other developed countries" like Japan and Australia and developing nations improved considerably.

The *WIR '04* has pointed out that apart from greater role of FDI activity, transnational company activity (TNC) has also picked up considerably over the years. UNCTAD's data show that international production is carried out by over 900,000 foreign affiliates of at least 61,000 TNCs worldwide.

Defining transnationality index of the host country as an average of four ratios — FDI inflows to gross fixed capital for 1999-2001, FDI inward stocks to GDP in 2001, value added of foreign affiliates to GDP in 2001 and employment of foreign affiliates to total employment in 2001— the Report has ranked Hong Kong as the most transnational country.

Within the developed country bloc, North America's inward performance index deteriorated sharply over the years to 0.45 in 2001-03 from 1.13 in 1988-90, due to slowdown in merger and acquisition activity, the Report said.

The developing countries improved their inward performance index from 0.99 to 1.25.

The *WIR '04* says that developed countries like Germany, United States and Japan have low values of outward performance index despite investing huge amounts outside in absolute terms.

This meant these developed countries have a long way to go before they reach the level of outward investment expected of them. The *WIR '04* adds that developing nations' FDI outflows have grown faster over the past 15 years than those from developed countries. "Negligible until the beginning of 1990s, outward flow from developing countries was 6 per cent of total world flow in 2003.

(*Business Standard*, 23 September 2004)

## PHDCCI Concerned Over Low Rate of FDI Inflow

THE PHD Chamber of Commerce and Industries (PHDCCI) has expressed concern over the low rate of inflow of FDI compared to the corresponding approval figures.

The PHDCCI is of the view that the percentage of cumulative actual FDI inflows compared to cumulative total approvals from 1991 to March 2004 is as low as 51 per cent, particularly because of delays caused at the state levels.

While policy barriers have been removed progressively and the time taken for clearing new proposals by the Foreign Investment Promotion Board (FIPB) has significantly come down, most of the delays are taking place thereafter.

This points to the need for an effective mechanism to improve cooperation and coordination between the Centre and the States in granting clearances, it said.

According to the analysis done by the PHDCCI, while inadequate infrastructure, lack of transparent guidelines and governmental delays are acting as bottlenecks to the entry of foreign investors, factors such as non-workability of BOOT (build-own-operate-transfer) and BOLT (build-own-lease-transfer) schemes are also holding up the progress.

The PHDCCI analysis shows that FDI inflows, which stood at $97 million in 1990-91, reached a peak of $3,557 million in 1997-98. In 2000-01, the FDI inflows were $4,029 million as compared to $4,675 million in 2003-04. Out of $4,675 million in 2003-04, the share of equity investment was $2,387 million, while reinvested earnings were placed at $1,800 million and inter-company debt transactions of FDI entities (other capital) stood at $488 million.

On the positive side, the analysis has pointed out that the realization rate of actual to approved FDI till 1997 was hovering around 30 per cent but eventually went up each year till 2001 when it stood at 71.7 per cent. Then onwards it jumped to 191.1 per cent in 2002 and 236.8 per cent in 2003 and finally to 317.5 per cent till March 2004.

According to the PHDCCI analysis, in order to attract greater inflows of FDI, the FDI policy of the country would have to be flexible, consistent, unambiguous and transparent with long-term objectives and with minimal mid-course policy changes to boost the foreign investors' confidence.

(*The Hindu Business Line*, 27 August 2004)

## Plans Afoot to Allow 100% FDI in Inland Water Transport Sector

THE Shipping Ministry has floated a plan to allow 100 per cent FDI in inland water transport (IWT) infrastructure and operations along with a host of fiscal and policy initiatives to popularize IWT as a viable mode of transport and ensure a modal shift from rail/road to this sector.

"Private investments in IWT sector will be encouraged along with 100 per cent FDI in IWT infrastructure and operations", says the policy for maritime sector drafted by the Ministry.

A Development Fund for IWT with a corpus of Rs 500 crore will be created at the national level. The existing subsidy scheme for the IWT sector will be re-examined and amended for restricting its scope to infrastructure and vessels and not for operations.

It is proposed to provide income-tax exemption for 20 years for investments made by companies in IWT infrastructure or IWT vessels. The rate of depreciation for IWT vessels will be made 5 per cent higher than the depreciation for ocean-going vessels.

Income earned by companies from IWT operations will be exempted from IT/corporate tax up to 100 per cent for 10 years and up to 50 per cent in next 10 years. It is also proposed to allow duty-free import of equipment, machineries, spares, installations, etc. for IWT development and operations.

To provide adequate cargo support, Government/PSU cargo would be moved by IWT. Suitable incentives are also proposed to be given to PSUs to encourage modal shift from rail and road to IWT. Specific projects for infrastructure development will be identified for implementation through joint venture/build-operate-transfer (BOT) route.

A dredging policy for inland water channels will be prepared and operationalized. Additional IWT terminals would be set up at potential locations and four-lane road connectivity as well as rail connectivity, wherever needed, would be provided for loading and evacuation of cargo.

Need-based cargo handling equipment and storage/warehousing space would be provided for which state governments would have to chip in with sufficient land free-of-cost. Navigational aids including night navigation facilities would be provided on all the three National Waterways within a year.

A scheme for fairway development and maintenance of each National Waterway will be prepared and implemented.

Currently, the share of IWT in India is only 0.15 per cent of the total inland cargo transportation in terms of tonne kms. "The proposed IWT policy seeks to increase this share to 2 per cent by 2025," says the policy paper acknowledging that IWT is an eco-friendly, cost-effective and fuel efficient mode of transport with huge potential for employment generation.

(*The Hindu Business Line*, 10 August 2004)

## C&W to Invest $10mn in India

THE UK-based Cable & Wireless (C&W) is planning to invest $10 million over the next 18 months in its India operations. The company would be investing $5 million towards its additional nodes and bandwidth, while another $ 5 million will be invested on employees and infrastructure.

"Since our inception in 1995, we have invested around $5 million towards establishing three nodes in Bangalore, Chennai and Mumbai. In the next 18 months, we would be investing in two additional nodes in Hyderabad and New Delhi," said company's Asia-Japan Chief Executive Officer, Mr. Phil Green.

The company also launched its multi-protocol label switching (MPLS) service in India as an extension of its managed data services portfolio in India, in association with Reliance Infocomm. "As the number of leading global companies setting up key business centres in India increases, there is more dependency on software companies and information technology enabled services (ITES) organizations, for seamless business continuity. With C&W MPLS, corporates can communicate with their employees, customers and suppliers around the world via a single IP network," said Mr. Green.

C&W had announced its managed data network in India earlier this year, and is now providing data services such as ATM, frame relay and managed private line to its customers in India.

(*EFE*, 5 August 2004)

## Regulator Keen on Interlined FDI Policy for Media Sector

AN interlinking FDI policy could be the next big thing for the media and broadcasting sector of the country. Chairman of the Telecom Regulatory Authority of India (TRAI) Pradip Baijal said that the issue is being examined. "We feel that there should be an interlinking FDI policy across news, entertainment, TV, cable, newspaper, magazines, radio….," Shri Baijal said, when asked about the direction of TRAI recommendation on FDI in private FM radio.

So far, the Information and Broadcasting Ministry has had a piecemeal approach towards the media sector, in the context of foreign investment. While stating that a view on FDI in a particular area of the sector is not correct, Shri Baijal was firm that "the entire media sector should be looked at together." That does not mean, however, TRAI would recommend the same FDI level all across the media sector, but that there should be some interconnect in the FDI policy.

At present, direct-to-home (DTH) broadcasting platforms are allowed FDI up to 20 per cent, news TV channels being uplinked from India 26 per cent, newspapers 26 per cent, speciality journals 74 per cent, cable networks 49 per cent, and private FM radio is not permitted any FDI at all. There's not unified policy on FDI for the sector yet.

Even as TRAI is not likely to offer a separate view on FDI in FM radio, it may have something more concrete to say about "news". Currently, news is not permitted in private FM, and TRAI may not recommend it either.

According to sources in the Government, the Home Ministry is of the view that "news" must not be permitted in private FM radio. The Home Ministry is understood to have cited security/law and order reasons for this view. Shri Baijal confirmed it, and added that "when the regulator makes a recommendation, he has to take all the views into account."

In DTH policy too, changes are expected. TRAI wants to make it mandatory for TV channels to give their content to all DTH providers on a non-discriminatory basis. "if this is not made mandatory, you as a consumer will be required to have multiple dishes," Mr Baijal argued. TRAI, which has the additional responsibility of the broadcasting sector, is expected to issue recommendations on FM radio and conditional access system (CAS) shortly.

(*EFE*, 5 August 2004)

## Asahi India Plans Expansion, to Invest Rs 600 cr

ASAHI India Glass is planning to invest about Rs 600 to 700 crore over the next few years towards capacity expansion and setting up new plants.

The company's new facilities would include two new processing plants and a float glass plant. "We would definitely require a new float glass plant over the next few years and setting up the same would require an investment of about Rs 400-500 crore", Sanjay Labroo, Managing Director and CEO of Asahi India Glass, said.

Further, the two new processing plants (which are set to come up in the North and the South) are to be modelled on the same lines as the architecture processing plant in Taloja, Maharashtra. The company intends to spend about Rs 50 crore towards the three processing plants.

Meanwhile, Asahi India's new plant in Chennai for automotive glass is to be commissioned in November this year. "The plant will be completed in phases. We plan to invest about Rs 170 crore in the plant, out of which Rs 54 crore would be invested in this fiscal", Shri Labroo said.

In other words, the new subsidiary would be used to promote greater use of value-added glass in buildings by increasing awareness among architects and users.

Per capita glass consumption in India is only about 0.56 kg a year, compared with China's 3.5 kg and 6 kg in Thailand. Only four per cent of the glass used by India's construction industry is treated (either glazed or laminated).

"We, however, expect this number to increase to 10 per cent over the next few years and the market to grow to about Rs 1,000 crore in this period", Shri Labroo said. Asahi India, a joint venture between Japan's Asahi Glass Co., Labroo family and Maruti Udyog Ltd. is targeting a sales growth of 15-16 per cent this year.

"The automotive segment will continue to drive sales for the company as the segment is growing at about 18-19 per cent. Further, we have a market share of about 90 per cent in this segment", he said.

(*The Hindu Business Line*, 4 August 2004)

## Global Insurers Waiting in Wings to Enter Indian Market

GLOBAL insurance majors such as Astra Insurance and Ace Insurance are waiting in the wings to enter the Indian market. The companies are likely to place their applications, seeking approval for setting up full-fledged operations, once the confusion over the hike in the FDI cap is settled.

However, prior to that they may set up their representative offices in India, for which they need the approval of the Reserve Bank of India. In addition to these two, the Holland-based Aegon Life Insurance, which earlier had a representative office in India, is also considering to re-enter the Indian market.

According to a senior analyst of the Federation of Indian Chambers of Commerce and Industry (FICCI) that the international insurance companies are looking at fresh and growing markets like India and China for future expansion. "The insurance market is saturating worldwide and therefore most companies are scouting for fresh markets. India and China among the growing markets offer huge potential," the analyst said.

(*The Financial Express*, 4 August 2004)

## Raise FDI Cap for Telecom Growth

THE Indian telecom story so far has been quite exciting. With the wireless market showing galloping growth over the past three years, the industry has achieved the tele-density target of 7, almost two years ahead of the time-frame set by the Government.

The Government has played a catalyst's role in bringing about this growth by reducing licence fees, ushering in more competition, introducing unified licencing, etc.

The industry players, on their part, have invested substantially in building up telecom infrastructure, adopted state-of-the-art technologies, as well as expanded and penetrated the market with their marketing strategies. The industry has attracted a significant quantum of FDI -- around $2.56 billion, which is around 13 per cent of the total FDI received by the country so far. Now what?

The next tele-density target of 15 by the year 2010 is before us. The challenge in achieving this will be far greater than the challenge faced in achieving a tele-density of 7. The industry has tapped an easy one-third of the telecom market, leaving a more difficult two-thirds yet to be tapped, which primarily comprises rural households.

To penetrate this market segment and sustain the same growth in tele-density, the industry requires huge investments, an estimated Rs 50,000 crore over the next three to four years. It's obvious that this kind of money cannot be raised from the domestic markets; so there is an undeniable need for more foreign investment in the telecom industry.

Raising the foreign investment limit to 74 per cent is critical to industry growth because it will enable Indian telecom companies to raise substantial amounts of funds from FIIs, who would be more than willing to invest in the Indian telecom growth story. Unlisted players will be motivated to raise funds for their expansion from the capital markets, including FIIs, through IPOs. Already Idea and Hutch are contemplating IPOs later this year. More may follow suit.

On the other hand, whether or not to have a sub-limit for FDI at 49 per cent within the overall foreign investment limit of 74 per cent is not as important an issue from the industry point of view. How many of the Indian telecom players would be really keen to increase the FDI shareholding in their companies beyond 49 per cent?

Hutch, definitely, so that it can dismantle the complicated holding structure it currently has, and route investment more directly into the operating company. Idea, perhaps, if the STT-Telekom Malaysia combine is interested in hiking its stake in the company, by buying out the Tatas and the Birlas, or through a fresh equity issue by Idea. The other players may not want to cede majority stake and management control to a foreign telecom company.

Therefore, it is vital that the Government increases the foreign investment limit in the telecom industry to 74 per cent. If the Government perceives a serious security issue in FDI shareholding exceeding 50 per cent, then it can create a sub-limit for FDI within this overall limit of 74 per cent.

However, in such a case, it is extremely important that the Government keep investment by private equity funds outside the definition of FDI.

(*The Financial Express*, 2 August 2004)

## WTO Framework A Major Victory: Kamal Nath

INDIA termed the WTO Framework Agreement as a major victory saying it had secured significant gains and succeeded in protecting its interests in agriculture and other key areas.

Commenting on the Agreement, the Commerce and Industry Minister, Shri Kamal Nath, said the revival of the Doha process benefited India.

Shri Kamal Nath, who spearheaded the developing nations' crusade against developed countries, said the adoption of a framework that met India's key demands aimed at preserving the country's domestic policy space. It provided for special products, and special safeguard mechanism and special and differential treatment with respect to market access.

The framework sets out the guidelines for further negotiations under Doha Round of Multilateral Trade Negotiations, encompassing the key areas of agriculture, non-agriculture market access, services and trade facilitation. It drops the three Singapore issues relating to *investment*, competition policy and government procurement from the Doha agenda, which led to the stalemate at Cancun leading to the collapse of the ministerial.

According to the statement, India's longstanding demand along with the G-33 developing nations for special products and special safeguard mechanism to protect the interest of farmers have been met.

The concept of proportionality, which requires lesser tariff reduction commitments from developing nations, was also a major gain for the country. The accepted tiered or branded approach takes into account the fact that the sensitivities of developing countries in agriculture such as the tariff structure were fundamentally different from that of developed nations.

(*The Hindu Business Line*, 2 August 2004)

## For A Few Dollars Less

EVEN before any of the big multinational banks could choose between converting their branch operations in India into subsidiaries, Reserve Bank of India (RBI) issued a draft proposal restricting FDI by a single promoter to 10 per cent.

Curiously, these proposals come at a time when China – the biggest market for banks in Asia – is opening up further. At present, a foreign bank is allowed to hold 20 per cent in a local Chinese bank, while the limit for a combined stake owned by foreigners is capped at 25 per cent.

Foreign banks have held stake in more than one bank. For instance, HSBC holds shares in three banks. Currently, foreign banks are not allowed to deal in local currency. However, to become a party to the WTO, China has agreed to phase out regulations, which should allow foreign banks to do everything that local banks can by the end of 2006.

In China, only those foreign institutions with assets of more than $10bn qualify to apply for a subsidiary licence or to get into a joint venture. To qualify for a branch licence the capital requirement is even more at $20bn. To engage in local currency business they need to have three years of business operations in China and profitability for two consecutive years prior to the application.

According to bankers, consolidation would result in banks seeking investors with deep pockets since local investors would not be able to come up with the kind of money that large banks are looking for.

The RBI appears to be moving against the tide, compared to other countries which hold an interest for foreign banks. Senior foreign bankers say that RBI's stance will act as disincentive and they will no longer be interested in picking up stakes in the private sector.

(*The Economic Times*, 21 July 2004)

## 100% FDI Attracts $1,636 mn Investment in Townships

FOREIGN investment in the integrated residential township sector is on a high growth path after the Central Government allowed up to 100 per cent FDI last year. So far $1,636 million worth of investment has been committed for the development of integrated townships with a minimum area of 100 acres.

"Although the policies governing investment in the sector are still restrictive in terms of preconditions for interested parties, major developers from South-East Asia and other regions have been active in joint ventures with domestic property developers to execute large township projects in major cities in India", said Anurag Munshi, Associate Director of Jones Lang Lasalle-India.

The first FDI project in India to get the nod (earlier this year) is a 100 acre residential township proposed for development in Delhi's suburban district Gurgaon. This project developed by Feed-bank Ventures, an infrastructure and property firm, in collaboration with Malaysian developers, Kontur Bintang and West-port, is estimated at $160 million.

Another Malaysian firm, LIM Berhad, is also involved in two projects – a 2,200 unit apartment project ($150 million) in association with Andhra Pradesh Housing Board (APHB) and a 500 acre integrated township ($150 million) in SAS Nagar in Mohali in Punjab with the Punjab Urban Development Authority.

Canada-based Royal Indian Raj International Corporation (RIRIC) is coming up with $791 million Royal Garden City, a fully integrated township development in Bangalore. When Royal Garden City is completed it would have designed transportation, utilities, environmental and other infrastructure spread across 20-square kilometre.

Two prominent projects in Bangalore and Chennai are coming up with the help of Singapore based developers Keppel Land and Lee Kim Tah Holding respectively.

(*The Economic Times*, 19 July 2004)

## How Much Indian is the Telecom Sector?

THE debate over raising the foreign direct investment in telecom from 49 to 74 per cent has thrown up an interesting question as to how Indian is the country's telecom sector and whether after five years of liberalization do we need foreign funds for achieving the tele-density targets.

First, look at numbers that point to the Indianess of the telecom sector. The largest two players in the country — Bharat Sanchar Nigam Ltd. and Reliance Infocomm — which together account for more than 70 per cent of the investment made in the telecom sector, are fully Indian companies. Together, the two companies have about 45 million subscribers of the total 70-million user base in the country.

The foreign investment made in the Indian telecom sector, about $2 billion post-liberalization, is just about 20 per cent of the total investments made in the sector. Reliance Infocomm and Tata Teleservices have made investments up to $4 to $5 billion. And if you take the investments made by the state-owned BSNL, which was about Rs 20,000 crore in the last year, then the investment made by foreign companies in India does look puny.

In comparison, countries like China has received FDI worth $52 billion, primarily in the manufacturing sector, despite being a relatively closed economy. That's equivalent to the investment needed by India over the next five years to take the subscriber base to over 200 million. Telecom analysts believe that it is likely to come by following the Government's decision to increase FDI cap from 49 to 74 per cent. Sanjay Mehta of Ernst & Young says: "Telecom is a capital-intensive sector and one needs foreign funds to fulfil the targets of tele-density. If anyone is worried about security concerns in involving foreigners in a crucial sector like communications, then there are other means to monitor and plug leakages."

However, if one were to remove BSNL, which has a 40-million subscriber base, from the overall investment picture, the foreign influence on the Indian communication sector looks impressive. More than 60 per cent of the booming mobile market is controlled by companies which have 49 per cent foreign stake, 100 per cent of the mobile handset being used in the market are foreign brands, 65 per cent of the call centre business is set up by multinational companies, 80 per cent of the telecom equipment market is dominated by European and American manufacturers and telecom has received the second largest foreign investment in the country after the oil sector. India is among the very few countries in the world where FDI cap is so high in the communications sector.

The biggest investment has been in the cellular segment. The top three private Global System for Mobile (GSM)-based companies Bharti Tele-Ventures, Essar-Hutchison and Idea Cellular have between 49 and 33 per cent foreign equity.

Investments to the tune of Rs 5,000 crore made directly in the cellular sector have been primarily by Hong Kong-based Hutchison Whampoa and Singapore Government's investment vehicle Temasek Holdings.

Even the smaller players BPL Communication and Spice Telecom, the cellular operator in Punjab, has 49 per cent foreign equity.

These five companies together account for about 22 million subscribers of the 29 million GSM users in the country. Even in the mobile handset segment, it's foreign brands such as Nokia, Motorola and Samsung ruling the market. Though no one has invested to set up a manufacturing unit in the country so far, with 100 per cent foreign equity allowed in manufacturing, most of the companies are actively looking at the option.

It's the same scenario in the telecom equipment side. Except for a few companies like ITI primarily catering to the fixed line switching requirements of BSNL, most operators prefer to import.

Of the Rs 10,000-crore FDI received by the Indian telecom sector, only Rs 1,500 crore has gone to the manufacturing segment over the last 15 years.

The only segment, other than cellular, which has received attention by foreign investors is the telecom software and call centre business where big names like Nokia, Ericsson, Alcatel, Motorola, GE, Convergys have set up base in the country.

According to Kiran Karnik, President, Nasscom, the interest shown by multinational companies in the BPO segment is good for the country as it not only brings in employment but also best practices and awareness about India's potential as an investment destination.

(*The Hindu Business Line*, 17 July 2004)

## Foreign Biotech Companies Keen on JVs

MANY overseas biotech companies participating in Bangalore BIO2004 have expressed interest in entering into joint ventures or setting up independent units in Bangalore.

Addressing at the concluding day of Bangalore BIO2004, M.K. Shankarlige Gowda, Karnataka IT&BT Secretary, said some of the investment is likely to be made in bio services and bioengineering segment. He said, German company MWG has recently set up its facility in a record 90 days. An MoU for Indo-German Technology Bridge between Karnataka Biotechnology Development Council, Frankfurt Innovation Centre, and International Technology Cooperation Network of the Federal Government of Germany was signed.

(*The Economic Times*, 15 July 2004)

## Thailand Entices Indian Investment

INDIAN companies in sectors like agro-industries, automotive parts and components, electronics, high-value services (logistics and software) and fashion products that include garments, jewellery, leather products have significant investment potential in Thailand.

Indian companies can also look forward to Thailand as an attractive gateway to ASEAN and Western markets, said Suchart Phisitvanich, acting senior executive advisor, Board of Investment (BOI) of Thailand, at an interactive meeting organized by Federation of Indian Chambers of Commerce and Industry (FICCI).

He said, Indian industries that are considered to be very strong are software, biotechnology and pharmaceuticals. "Therefore, these industries qualify for the recently announced 'skilled technology and innovation' project promotion programme by BOI and are entitled to the best incentives and privileges for investment in Thailand, which is also one of the trading partners of India."

"Thailand is investor-friendly and the geographical location and liberal investment policy qualify the country as an attractive gateway not only to ASEAN countries but also to the Western markets." BOI proposes to offer a number of investor-friendly supports to investors including guarantee against nationalization and price control, permission to own land and bring in foreign expert, etc.

(*The Financial Express*, 15 July 2004)

## FDI Hike to Trigger M&As in Telecom

MERGERS and acquisitions (M&As) in telecommunications are expected to gather momentum after the Government's decision to hike foreign direct investment cap in the sector to 74 per cent from the existing 49 per cent.

"The move will fuel consolidation in the industry and lead to long-term players providing better quality services and absolute value to the consumer. It also makes India an attractive destination for investment to foreign investors," Sudhir Mathur, CFO, Idea Cellular Ltd, said.

At present, all private cellular service providers are partially owned by foreign investors. While SingTel owns 28.5 per cent of India's largest GSM operator Bharti Tele-Ventures, the second largest player Hutch is 42 per cent owned by Hong Kong's Hutchison Telecom International.

A consortium of Singapore Technologies Telemedia and Telekom Malaysia recently acquired a 33 per cent stake in Idea Cellular, that was previously owned by US wireless major AT&T.

After the proposal to hike FDI comes into force, it will be possible for these foreign investors to increase their stake in these companies. With the existing foreign investors, many other investors from abroad are also expected to buy stakes in the Indian cellular companies.

"The sector will witness dramatic situations in terms of a number of mergers, acquisitions, consolidations and external capital market transactions," said Munesh Khanna, MD, NM Rothschild.

With more and more foreign funds, the cellular industry, that is reeling under an accumulated loss of about Rs 7,000 crore, will get adequate funds to undertake expansion plans to meet the growing demand of increasing lines.

(*Business Standard*, 12 July 2004)

## Market Conditions to Hurt FDI Flow, says FICCI Survey

WHILE security and terrorism concerns weigh heavily on the minds of foreign investors, factors like exchange rate volatility, hardening commodity prices and higher interest rates in their home countries may spoil the parity as far as investment inflow into India is concerned, according to Federation of Indian Chambers of Commerce & Industry (FICCI).

"Ground level hassles continue to be a major impediment for foreign investors. A substantial 88 per cent of respondents have said that ground level hassles in India are medium to high," FICCI stated in its *Foreign Direct Investment Survey 2004*.

As far as infrastructure facilities in the country are concerned, there is still a lot of room for improvement. "Transport, roads, power and water availability have been rated as 'bad' by majority of the respondents," it said.

The quality of services being offered at ports and airports still leave a lot to be desired. "No wonder 43 per cent and 42 per cent of the respondents respectively finds port and airport facilities in India to be below international standards," it added.

The time consuming procedures and systems to be complied with often lead to time and cost overruns, which is bothering the investors. Procedural delays have been rated as "quite to very serious" by 93 per cent of respondents.

About 69 per cent of respondents have assessed problems on account of the existing labour laws to be "quite to very serious".

The survey, however, revealed an improvement in the perception of foreign investors with regard to the operational parameters and the prevailing market conditions in India. The survey has identified five thrust areas where a dedicated effort by the

Government would result in strong FDI inflows in the near to medium term. "These include information technology and related services, chemical & chemical products, rubber & plastic products, electrical machinery & apparatus and services sector. A large proportion of respondents from the aforementioned sectors have assessed India favourably as an investment destination, perceive opportunities for greater FDI in their industry and are planning expansion of their Indian operations," the survey said.

(*The Financial Express*, 28 June 2004)

## MIGA Provides $12.5 bn Guarantee for Investment Projects

BUSINESSES today increasingly recognize that promising investment opportunities exist in emerging economies. But concerns about uncertain policy environments and perceptions of political risks, as well as a lack of awareness of specific opportunities, often inhibit investment. As a result, most foreign direct investment—a key driver of economic growth—goes to only a handful of countries, leaving the world's poorest people largely ignored.

The Multilateral Investment Guarantee Agency (MIGA), created in 1988 as a member of the World Bank Group, addresses these concerns in two ways: by offering political risk insurance (guarantees) to investors and lenders, and by providing technical assistance to help emerging economies attract private investment.

Since its inception, MIGA has provided $12.5 billion in guarantees for investment projects in 85 developing countries and facilitated an estimated $51.1 billion in additional FDI in poorer countries. These guarantees protect investments against the risks of currency inconvertibility and transfer restrictions, war and civil disturbance (including terrorism and sabotage), expropriation, and breach of contract. As of December 2003, MIGA's gross exposure was $5.3 billion.

MIGA provides coverage for projects in virtually all sectors, ranging from tourism to telecommunications, and from banking to manufacturing. Insurance is particularly important for large, capital-intensive projects in the energy, mining, heavy industry, and infrastructure sectors.

Projects eligible for coverage include new, cross-border investments originating in any member country and destined for any developing member country. Eligible forms of investment include equity, shareholder loans, and loan guarantees issued by equity holders, as well as technical assistance, management contracts, leases, franchising and licensing agreements, and performance bonds. MIGA also insures loans by unaffiliated financial institutions, such as commercial banks.

*(www.worldbank.org)*

## World Bank Agrees to Continue Oil, Gas Lending

THE World Bank has agreed to continue making investments in oil, gas and mining, setting aside an independent review's recommendations that it phase out lending for such projects.

The Bank's board of directors lent its support to a previously disclosed management proposal to encourage selective investment in extractive industries, including a greater focus on how projects may impact local communities.

"The proposals of management are built around the central theme that our investments and policy advice in the extractive industries should benefit the poor first and foremost," said World Bank President James Wolfensohn.

Mr. Wolfensohn had in 2000 commissioned an independent review of the Bank's support for the extraction of oil, coal, gold and natural gas in poor nations, following concerns the lender was contributing to poverty instead of easing it.

The review, led by Indonesia's former Environment Minister Emil Salim, recommended the Bank radically change its approach to funding such projects and even stop supporting some. Mr. Salim had called for an end of oil-related loans by 2008.

The World Bank Group's management responded in June by saying it would continue to fund oil, gas and mining projects but would require high environmental and social standards. It also said, it would boost its support for environmentally friendly renewable energies and clean energy sources like natural gas.

Mr. Wolfensohn said that energy and mining resources are essential to many poor countries' development goals, and should not be excluded from the Bank's remit. "The harsh reality is that some 1.6 billion people in the developing nations still do not have electricity, and some 2.3 billion people still depend on biomass fuels that are harmful to their health and the environment," he said in a statement. "That underscores the need for our continued but selective engagement in oil, gas, and coal investments."

Rashad Kaldany, Director of the World Bank Group's oil, gas, mining and chemicals department, pointed to the Bank's decision to disclose more information about revenues and evaluative measures as a sign of real progress. "This is a large and very significant step forward," he said. "This is at the very least a cultural change that will be required. We will have to be very explicit in public on what we expect to accomplish through these projects." The World Bank Group lends about $500 million to $600 million per year - about 3 per cent of its total commitments - on extractive industries projects, Mr. Kaldany said.

In the past year, World Bank affiliates helped fund two criticized private sector oil projects - the Chad-Cameroon and the Baku-Tbilisi-Ceyhan pipelines - which both carry crude thousands of kilometres overland to the sea.

(*Reuters*, 2004)

## Expanded Trade and Investment Holds Promise for Millions of Jobs in the Middle East

WORLD BANK report calls for sweeping reforms to fight poverty, unemployment. The countries of the Middle East and North Africa (MENA) could ward off a major unemployment crisis in the coming years by expanding trade and private investment and generating millions of new jobs according to a World Bank report, *Engaging with the World: Trade, Investment and Development in MENA* warns that the *status quo* — public sector-driven and protected economies supported by oil, aid and workers remittances — can no longer generate sufficient growth or jobs, as the experience of the past two decades suggest. Instead, it calls on countries to embrace trade and investment reforms, which promise much faster growth and much needed employment opportunities in the region.

"The region has enjoyed greatest prosperity when it has been open to trade, ideas, innovation and private enterprise, and exploited its potential of location, endowments and spirit of enterprise," says Jean-Louis Sarbib, Vice-President for the Middle East and North Africa Region at the World Bank.

*(www.worldbank.org/mena)*

## IFC Promotes Sustainable Private Sector Investment

INTERNATIONAL Finance Corporation (IFC) promotes sustainable private sector investment in developing countries, helping to reduce poverty and improve people's lives.

IFC is a member of the World Bank Group and is headquartered in Washington, DC. It shares the primary objective of all World Bank Group institutions: to improve the quality of the lives of people in its developing member countries.

Established in 1956, IFC is the largest multilateral source of loan and equity financing for private sector projects in the developing world. It promotes sustainable development primarily by:

- Financing private sector projects.
- Helping private companies in the emerging markets mobilize financing in international financial markets.
- Providing advice and technical assistance to businesses and governments.

IFC's focus is to promote economic development by encouraging the growth of productive enterprise and efficient capital markets in its member countries. In this context, the advisory work with governments helps create conditions that stimulate the flow of both domestic and foreign private savings and investment.

IFC participates in an investment only when it can make a contribution that complements the role of market operators. Accordingly, it plays a catalytic role, stimulating and mobilizing private funding by demonstrating that investments can be profitable even in challenging environments. IFC operates on commercial terms, investing only in projects with the prospect of being profitable. The Corporation has made a profit every year since its inception.

### Investment Operations for Fiscal 2004

IFC signed investment commitments of $5.63 billion for 217 projects in FY04, of which $880 million were mobilized through loan syndications. Of the investment commitments IFC signed for its own account, $3.40 billion were for loan agreements, $787 million were for equity investments, $339 million were for quasi-equity investments, $171 million were for structured finance products (including guarantees), and $60 million were for risk management products. Almost 64 per cent of the new investments were in IFC's five priority sectors: the financial industry, infrastructure, information technology, small and medium enterprises, and health and education. The share of investments in frontier countries—either high risk or low income—was 22 per cent.

Based on total project costs for FY04 projects, each $1 in IFC commitments for its own account resulted in an additional $5.14 in funding from other sources.

IFC's investment portfolio at June 30, 2004, included $17.9 billion in investments for IFC's own account and $5.5 billion in syndicated loans held for others.

### Project Finance

IFC offers an array of financial products and services to its client companies:

- Long-term loans in major currencies, at fixed or variable rates
- Equity investments
- Quasi-equity instruments (subordinated loans, preferred stock, income notes)
- Structured finance, including guarantees and securitizations
- Risk management tools.

To be eligible for IFC financing, projects must have the prospect of being profitable for investors, benefit the economy of the host country, and comply with stringent social and environmental guidelines. IFC finances projects in commercial sectors including infrastructure, financial services, manufacturing, tourism, and many others. To ensure the participation of investors and lenders from the private sector, IFC limits the total amount of debt and equity financing it will provide for any single project to 25 per cent of total estimated project costs; it will not normally hold more than a 35 per cent stake or be the largest shareholder. IFC investments typically range from $1 million to $100 million.

### Mobilization

Due to its record of success and special standing as a multilateral institution, IFC can act as a catalyst for private investment. Its participation in a project enhances investor confidence and attracts other lenders and shareholders. IFC mobilizes financing directly for sound companies in developing countries by syndicating loans with international commercial banks and underwriting investment funds and corporate securities issues. IFC also offers partial credit guarantees of debt instruments and other structured finance solutions to clients, helping them diversify their funding sources, extend maturities, and obtain financing in their currency of choice.

### Advice and Technical Assistance

IFC advises businesses in developing countries on a variety of matters, including:

- Restructuring;
- Business plan formulation;
- Identification of markets, products, technologies, and financial and technical partners; and
- Mobilization of project finance.

It can provide advisory services in the context of an investment, or independently for a fee, in line with market practice. It also advises governments on improving the environment for private investment, developing domestic capital markets, restructuring and privatizing state-owned enterprises, and attracting foreign direct investment.

*(www.ifc.org)*

# BOOKS/ARTICLES NOTES

## BOOKS

**Policy Impediments to Trade and FDI in India**
by B. Bhattacharyya and Satinder Palaha, Indian Institute of Foreign Trade, Wheeler Publishing, New Delhi, 1996.

THE publication makes an attempt to develop a consensus on the unfinished agenda for reforms relating to trade and FDI. It presents a summary of 24 reports dealing with foreign trade and FDI. These reports were prepared for a USAID-funded Project titled "Policy Impediments to Trade and FDI in India".

The publication says that there has been substantial improvement in the FDI inflows to India. For further boosting FDI in the country, it makes some suggestions. Among these, the major ones include: (i) At the entry level, the number of alternative routes should be reduced to two, viz. the Automatic Approval (AA) Route to be cleared by RBI and the Foreign Investment Promotion Board (FIPB); (ii) The Policy framework should be liberalized to make the AA route more effective; (iii) The current institutional set-up in India does not provide a mechanism for attracting FDI. The Government may look into the matter and announce appropriate steps in this direction. The FIPB, despite its name, in reality, works merely as a clearance mechanism. The Indian Investment Centre, on the other due to its having no overseas offices, is not in a position to attract FDI from abroad. Finally, the publication lays emphasis on evolving a mechanism for fostering close linkages with the private sector as an integral partner.

**Proceedings of the Seminar on Negotiations Techniques in the Area of Trade and Investment Liberalization,** Indian Institute of Foreign Trade, June 2000.

THE publication highlights proceedings of the Workshop on Negotiation Techniques in the Area of Trade and Investment Liberalization. The Workshop was organized by the Indian Institute of Foreign Trade and was sponsored by the Ministry of Finance, Department of Economic Affairs, Government of India; Norwegian Agency for Development Corporation (NORAD), Oslo, Norway; and the Colombo Plan Secretariat, Colombo (Sri Lanka) from 26-30 June 2000 at New Delhi. Subjects covered in the Workshop included: "Development in International Negotiations, Trade and Tariffs Negotiations", "Multilateral Investment Agreements", "Multilateral Environmental Agreements", "Dispute Settlement System", and "National Capacity Building".

The publication contains a set of papers which were presented at the Workshop both by the Indian and foreign experts. The papers presented by the foreign experts included representatives from Bangladesh, Bhutan, Cambodia, Indonesia, Iran, Laos, Mongolia, Myanmar, Pakistan, Papua New Guinea, Sri Lanka and Thailand. These papers focus on the political aspects of trade talks with special reference to trade negotiation techniques. This, it says, will help sharpen the skills of policy-makers in trade negotiation techniques and make the negotiations more productive and fruitful.

**Foreign Direct Investment for Development: Maximizing Benefits, Minimizing Costs**, Organization for Economic Cooperation and Development, Paris (France), 2002.

THE publication consists of eight chapters. Chapter I discusses recent FDI trends in OECD and non-OECD member countries. Chapter II looks at the overall impact of FDI on economic growth. Chapter III reviews the linkages between FDI and foreign trade, with special reference to the role of FDI as a catalyst for economic growth through trade integration. Chapter IV examines the effects of FDI on human capital formation in the host economy. Chapter V examines the impact of FDI on competition in the host-country business sector. Chapter VI studies the impact of FDI on enterprise restructuring and corporate governance. Chapter VII presents empirical evidences of the linkages between FDI and non-economic variables such as social and environmental indicators. The concluding chapter, on the one hand, reviews policy developments which impacted FDI trends in the past decade and on policy requirements to maximize benefits from the FDI, on the other.

**New Horizons for Foreign Direct Investment**
by Mehmet Ogicil and Franco Benois, Organization for Economic Cooperation and Development, Paris (France), 2000.

THE publication says that the benefits of FDI do not accrue automatically and are not uniform in different sectors and countries. The Government needs to pay more attention to evolving a broad set of regulatory and institutional measures conducive to an enabling environment both for FDI and domestic entrepreneurship. Some of the measures suggested in the publication include: more transparent administrative practices, good corporate governance, sound competition policy and protection of labour and environment. In its concluding remark, the publication calls for establishing strong partnerships to capacity-building to attract FDI.

**Enlargement, Trade and Investment: The Impact of Barriers to Trade in Europe**
edited by Paul Brenton and Stefano Manzocchi, Centre for European Policy Studies, Edward Elgar, MA (USA), 2002.

IN its opening remarks, the publication says that FDI plays an important role in the development process of a country and has emerged as an integral part of economic prosperity. FDI, it says, enables investors to look beyond the constraints of their domestic investment environment and gain access to resources and bigger markets, and maximize their investment returns. Further, it provides, an analysis on FDI regulations. Finally, it lays emphasis on adopting a pragmatic global regulatory framework which may help to solve the resulting problems from the multilateral investment agreement.

**Bilateral Investment Treaties in the Mid 1990s**,
United Nations, Geneva, 1998.

THE publication comprises five chapters. Chapter I reviews the objectives of bilateral investment treaties and their origins, evolution and geographical distribution and recent trends. Chapter II discusses the negotiating process of the investment treaties. Chapter III analyzes individual clauses in bilateral investment treaties, focussing, in particular, on the terms and principles involved, how these are used, the differences and similarities between the present and former treaty practices, and the implications of individual treaty provisions for development. Chapter IV examines the impact which the bilateral investment treaties have on investment flows. The concluding chapter summarizes the main conclusions. The publication also contains two Annexures. While Annexure I includes a list of bilateral investment treaties signed on 1 January 1997, Annexure II reproduces select model treaties of some countries or groups of countries.

**Foreign Investment in India: Liberalization and WTO–The Emerging Scenario** by Chanchal Chopra and Dr. A.K. Seth, Deep & Deep Publications, New Delhi, 2003.

THE book examines the trends and patterns of foreign investment in India in the pre and post liberalization periods *vis-a-vis* the major policy changes. It has been presented in 14 chapters. Chapter I highlights the unprecedented changes of the 'eighties and 'nineties in the global resource flows. Chapter II speaks about the significance of foreign investment in emerging market economies. The chapter also discusses regional and sectoral distribution of portfolio flows. Chapter III studies the impact of FDI on financial resources and investment, enhancing technological capabilities, boosting export competitiveness, generating employment and strengthening the skill base of the host countries. Chapter IV outlines salient features of the prevailing policy environment in the country. Chapter V discusses procedures adopted for annual approvals of foreign collaborations, distribution of FDI inflows by country sources, major industrial sectors and by major recipient states of India. Chapter VI deals with NRIs' investment and deposits in India, the adequacy of incentives, repatriation facility, tax exemptions and the impact of interest rates. Chapter

VII studies the growing importance of FII investment in the post-liberalization period. Chapter VIII analyzes global depository receipts (GDRs) in the emerging post-liberalization era. Chapter IX focuses on external commercial borrowings (ECBs) by India as an additional and important source of external finance. Chapter X deals with tax-related issues in foreign investment, viz. impact of double tax avoidance treaties on the FDI approvals, long-term capital gains in India and other countries. Chapter XI focuses on the determinants of FDI inflows in India. Chapter XII deals with the impact of the FDI on Indian economy in the light of national technological capability, export performance and foreign exchange inflow. Chapter XIII analyzes the WTO Agreements on TRIMs, GATS and TRIPs which directly impact the inflow of FDI into a country. The concluding chapter summarizes the main observations and conclusions and makes some suggestions to the policy-makers.

**Promotion of Trade and Investment in Eastern South Asia Sub Region (ESAS)** edited by Jayanta Kumar Ray and Prabir De, Bookwell, New Delhi, 2001.

THE publication contains a set of papers which were presented at an international workshop held at Kolkata on 18-19 October 2001. The Workshop was organized by South Asia Research Society with the support from the Ministry of External Affairs, Government of India. The publication underlines the need for effecting large-scale administrative reforms for promotion of investment and trade in the ESAS.

The book points out that attracting investments to the ESAS from non-ESAS sources for mega projects, e.g. highways, hydro-power, etc. may need joint efforts by the public and private agencies in the ESAS countries. Whereas the Asian Development Bank has already announced various initiatives in this direction, much more still needs to be done by ESAS countries to attract investments from countries like Japan, Europe and North America.

Finally, the publication calls for the public and private sector agencies in ESAS countries to pool their resources for initiating a comprehensive and systematic entrepreneurship development programme. If such entrepreneurs in ESAS countries can provide original products in some sectors, viz. information technology, biotechnology, and solar/wind energy, they will substantially contribute to poverty alleviation, growth, investment and trade.

**Liberalizing Foreign Direct Investment Policies in the APEC Region** by Bernie Bishop, Ashgate, USA, 2001.

THE publication has been organized in four chapters. Chapter 1 provides a historical perspective of investment liberalization in the APEC region. Chapter II discusses the economic and political constraints for further liberalization in the APEC region. Chapter III looks at the investment liberalization of the APEC. Chapter IV examines policy measures in a more liberalized investment environment. The chapter opines that rather than fiscal incentives, improvements in corporate governance may be more effective in attracting investment.

**Trade Liberalization and Foreign Investment in India: 1991-2001** by Vibha Mathur, New Century Publication, New Delhi, 2000.

THE book has been presented in eight chapters. Chapter I examines the trade policy regime in India during the pre-liberalization period. Chapter II discusses radical reforms introduced in the export-import policy during 1991-2001. Chapter III analyzes trends in the commodity composition and direction of trade. Chapter IV reviews policy measures introduced by the Government to promote exports. Chapter V describes the background against setting up of the WTO and examines its impact on the economies of developing countries. Chapter VI explains FDI policy of the Government of India. Chapter VII presents a sectoral analysis of foreign investment in India. The concluding chapter highlights prospects of foreign investment in India in the infrastructure sector.

**Legal Systems As A Determinant of Foreign Direct Investment: Lessons from Sri Lanka** by Amanda Perry, Kluwer Law International, London (UK), 2001.

THIS publication focuses on a case study of Sri Lanka relating with its foreign investors. The study focuses upon those foreign investors who were in commercial operations in Sri Lanka. These investors were preferred to those who were not in commercial operations since the latter had no experience of the Sri Lankan legal system. The study also focuses on those foreign investors who enjoyed priority status in Sri Lanka. The study says, that the Government of Sri Lanka grants priority status to investments which are export-oriented and are included in pre-defined sectors. The study further says that priority status companies are granted many tax incentives.

**Foreign Direct Investment, Regional Economic Integration and Industrial Restructuring in Asia: Trends, Patterns and Prospects** by Nagesh Kumar, Research and Information System for the Non-Aligned and Other Developing Countries, (RIS), 2001, New Delhi.

IN its introductory remarks, the publication says that FDI has emerged as an important agent of efficiency seeking restructuring of industry across countries. Against this background, it reviews the recent trends and patterns of global FDI flows relating to Asian developing countries. Subsequently, it examines the emerging patterns of industrial restructuring in different parts of the world. Further, it discusses prospects of the poorer Asian countries. Later, it deals with the progress of the regional economic integration in the South East and South Asian countries. Finally, It summarizes major conclusions and findings.

**Investment Regimes in the Arab World: Issues and Policies**, United Nations, New York and Geneva, 2000.

THE publication says that the FDI in developing countries increased rapidly in the 1990s and has emerged as a principal channel for the transfer of long-term private capital, technology and managerial know-how, as well as forging a link between national economies and the world market. The Arab countries, it says, welcome FDI and have been successful in attracting foreign investors. However, FDI flows to the Arab world, as a whole, remain modest and have not kept pace with the global trend. There are many reasons for the low level of FDI flows to the Arab countries. One important reason is the general deficiencies and shortcomings of the legal and institutional framework in many countries. The publication mentions that legal and institutional framework for investment is a necessary first step for effecting harmonization of laws and regulations in these countries. Arab countries have improved their policies relating to FDI. But the investment framework still remains patchy. In order to attract investment, these countries need to ensure fair treatment to all investors.

The publication has been organized in three parts. Part I provides an overview of the main issues and challenges facing the Arab world with respect to regulatory and institutional framework for investment. Part II deals with different case studies relating to investment of some countries. The concluding part deals with settlement of disputes and financial governance.

**World Investment Directory: Foreign Direct Investment and Corporate Data**, Vol. VII, Part I, Asia and the Pacific, United Nations, New York and Geneva, 2000.

THE publication presents profiles of 41 economies of the Asia and Pacific region. The profiles contain information on inward and outward flows of FDI, their relative importance to host and home economies, and basic financial data on the major transnational corporations in these countries. The data given pertain to 1999. The World Investment Directory can be found useful for policy-makers, as well as researchers in academia, government, inter-governmental and non-governmental organizations and the private sector, who need to gain an understanding of the character, pattern and trends of FDI and require reliable information as the basis for the formulation and monitoring of policies relating to foreign investment and transnational corporations.

**China's Trade and Investment After the Asia Crisis** edited by Tran Van Hoa, Edward Elgar, MA (USA), 2000.

THE publication has been presented in nine chapters. Chapter I deals with the trends and patterns of China's trade by country of destination and origin. Chapter II deals with various issues related with FDI in China. Chapter III examines different aspects of China's trade including the WTO, and APEC and the North East Asia Economic Cooperation (NEAEC). Chapter IV explains China's investment issues. The issues involve domestic capital supply and FDI by the small and medium-sized enterprises. Chapter V gives an account of the successful small and medium enterprises in Hong Kong. Chapter VI deals with China's trade with Australia. Chapter VII speaks about China's development at the macro level and its implications for trade in the coming years in the light of its membership to the WTO in the near future. The chapter also reviews the recent macro-economic developments, structural problems and potential risks to China's economic stability. Finally, the chapter discusses the policy response to these macro-economic developments and its potential impact upon China's international trade. Chapter VIII highlights problems of China's trade and investment in the first decade of the twenty-first century, as assessed by experts.

**Technology for Development Series Investment and Technology Policies for Competitiveness: Review of Successful Country Experiences** UNCTAD, United Nations, New York and Geneva, 2003.

THIS publication was prepared as a background note for the Panel of the United Nations Commission on Science and Technology for Development on "Linking FDI, Technology Development for Capacity-building and Strategic Competitiveness", which met in Colombo (Sri Lanka) from 15 to 17 October 2002. The note discusses technological capabilities and enhancing competitiveness. It also highlights the important role played by FDI in effecting transfer of technology. Further, based on its evaluation of the case studies of South-East Asian countries, it discusses some strategies used to build domestic capabilities.

**Attracting International Investment for Development,** OECD Global Forum on International Investment, OECD, 2003.

THE publication contains a set of papers which provide insights for the policy-makers and the companies engaged in FDI. One of the problems highlighted in these papers related to the relatively low volume of FDI in the least developed countries is owing to the fact that these countries have poor infrastructure facilities, low endowments of human capital and the absence of effective corporate structures and meaningful macro economic policies, all of which are essential ingredients for successful utilization of FDI in the development process. Further, these papers makes an attempt to find alternatives to FDI and ways and means of forging complementarities between FDI and other forms of capital flows.

**The Development Dimension of FDI: Policy and Rule-Making Perspectives,** UNCTAD, New York and Geneva, 2003.

THE publication contains proceedings of the Expert Meeting held under the aegis of UNCTAD at Geneva from 6-8 November 2002. FDI, it says, can play a significant role in host economies' development process. In addition to capital inflows, FDI can also prove to be a vehicle for obtaining foreign technology, knowledge, managerial skills and other important inputs integrating into international marketing, distribution and production networks; and improving the international competitiveness of firms and the economic performance of countries.

It has been organized in three sections. Section 1 discusses the role of FDI-related host country policies. Section 2 looks at the potential role of home country policy measures. Section 3 addresses the role of safeguards and the rights of the host governments to regulate these measures.

**The World Investment Report,** UNCTAD, United Nations, New York and Geneva, 2003.

THE publication says that FDI helps in many ways, viz creating jobs, raising productivity, enhancing exports and transfer of technology. Further it says that getting benefits from FDI is not always a *laissez faire* approach towards FDI. Attracting FDI requires locational advantages and focused efforts on its promotion.

Speaking about the FDI trends, it highlights that global FDI has declined significantly from $1.4 trillion in 2000 to $650 billion in 2002. Global FDI inflows declined by 21 per cent in 2002. The main factors towards declining trend of FDI include (i) lower corporate profitability, (ii) slowdown in the pace of corporate restructuring in some industries, and (iii) the winding down of privatization in some countries. The publication also discusses promotional strategies followed by some countries to attract FDI.

The publication is organized in two parts. Part I provides information on findings of various studies on FDI and transnational corporations (TNCs). Part II makes an analysis of FDI policies in select countries.

# ARTICLES

**Multilateral Investment Agreement in the New Era of FDI: Implications for India and Other Emerging Market Economies** By Thomas L. Brewer, *Foreign Trade Review*, Indian Institute of Foreign Trade, January-March 1995, pp. 254-276.

THE article has been presented in four sections. Section I describes status of FDI issues, their implications on India and other emerging economies. It also discusses prospects for future negotiations on FDI-related issues in the WTO. Section II deals with the negotiations held on a Multilateral Agreement on Investment under the aegis of the OECD. Section III highlights FDI issues at the WTO agenda. The concluding Section IV analyzes implications for India and other emerging market economies pertaining to FDI.

**Multilateral Agreement on Investment (MAI): What Should be the Response of the Developing Countries** by V.R. Panchamukhi, South Centre, Geneva, August 1996.

THE article makes an attempt to assist the developing countries in the task of evolving their own perceptions about Multilateral Agreement on Investment (MAI). It provides an inventory of guidelines which may enable the countries to prepare their own strategies to deal with MAI.

Further, the article examines various issues such as: "What has been the impact of the foreign investment flows on the different dimensions of the development process in the different countries under diverse investment regimes"?, "Is foreign investment sufficient for development"?, "Are all foreign investment flows necessary for development"? and "Why should a liberal trade regime be consistent with a managed foreign investment regime"?

Finally, the article stresses the need for adopting an approach of partnership and understanding, keeping in view the interests of all the parties.

**MAI** by Bibek Debroy and P.D. Kaushak, Chartered Accountant, Institute of Chartered Accountants of India, New Delhi, March 2000, p. 35.

THE article discusses about the efforts made towards reaching a Multilateral Agreement on Investment (MAI) both within and without the WTO. Foreign investment, it says, is a major issue in the TRIMs agreement. Some countries, however, are pushing it for a separate MAI. MAI was negotiated in areas such as direct investment, portfolio investment, real estate investment and rights under contract. Once it came into force, it aimed to provide a level playing field between foreign investors and their domestic counterparts. The proposed agreement allowed member governments to regulate their investment policies in accordance with the prescribed set of rules. The MAI aimed at eliminating all barriers to free movement of capital.

It also mentions that one common drawback to foreign investment is that it is foreign and accountable to the WTO sets of rules. Foreign investment entails a higher risk, but with that comes the possibility of better returns. Most foreign investment has either been the result of someone taking a huge risk or it has been underwritten by an international organization like the World Bank. Traditionally, foreign investment has been closely linked to trade or an international development agency.

The issue of MAI, it says, was raised at the Singapore Meet. Subsequently, a Working Group on Trade and Investment was constituted within the WTO. The proposed MAI has become a guiding tool for the Committee which is looking into trade and investment.

In its concluding remark, it says that the MAI is seen largely as a complement to the WTO agreement for trade and investment facilitation. The shift of focus from products to services could lead to a more aggressive stand taken by the developed nations.

**WTO Regime, Host Country Policies and Global Patterns of MNE Activity: Recent Quantitative Studies and India's Strategic Response** by Nagesh kumar, *Economic and Political Weekly*, Vol. XXXXVI, Nos. 6-12, January 2001.

THE article analyses the role of structural, geographical and policy factors in shaping the patterns of MNE activity. The focus is on the role of host government policies and on the implications of the emerging WTO regime.

The article has been presented in seven sections. Sections I gives a brief introduction on the role of multinational enterprises (MNEs) in attracting FDI flows. Section II outlines frameworks that have been developed to analyze the patterns of FDI in the light of host government policies. Section III presents a summary of findings pertaining to the host government policy factors. Section IV discusses the implications of the emerging WTO regime for countries like India. The concluding section looks at India's response to the emerging challenges and stresses that developing countries should exploit the decisions arrived between the OECD countries on the investment issue that surfaced in the course of MAI negotiations to their advantage and buy some time in the process to study its implications. For that to happen, it says, unity of the developing countries will be of critical importance.

**The Doha Investment Negotiations: Whither or Wither** by Bill Dymond and Michael Hart, *The Journal of World Investment & Trade*, Vol. 5, No. 2, April 2004, Geneva, pp. 263-288.

THE article makes a review of some multilateral investment agreements in the past. WTO negotiations, it says, should aim to complement and strengthen the network rather than replace it. The WTO members need to accept that investment flows are affected by different factors and considerations rather than the exchange of goods and services. As such, these require a different set of rules and procedures than these which applied to trade in goods. Finally, WTO members need to accept that pursuing special and differential treatment for developing countries, which has already done immeasurable harm to the interests of developing countries in the context of trade in goods, is more perverse and counterproductive in the context of investment rules.

**To What Extent Can Foreign Direct Investment Help Achieve International Development Goals?** by Peter Nunnenkamp, *The World Economy*, Vol. 27, No. 5, May 2004, Blackwell Publishing, Oxford (UK), pp. 657-678.

THE article provides a review of the role of FDI in promoting economic development of Third World economies. It has been organized in five sections. Section I gives a brief introduction about the subject. Section II speaks about the significance of FDI as a source of development financing. Section III says that benefits of FDI are distributed unevenly among developing countries. Section IV says that for FDI to help reduce poverty and raising average incomes, two conditions need to be met. *First*, developing countries need to be attractive to foreign investors. *Second*, the host-country's environment must be conducive to favourable FDI effects with regard to overall investment, economic spillovers and income growth. The section further says that in the absence of a quick fix to deriving more benefits from FDI, policy-makers should not expect too much from FDI. For some countries, it may take more time to reach the minimum level of economic development. The international community, too, should be aware that FDI does not provide a panacea for the most pressing development problem, i.e., the high incidence of poverty in many developing countries.

**India-ASEAN investment Flows: Policies and Trends,** by T.P. Bhat, *Foreign Trade Review*, July-December 2000, Vol. XXXV, Nos. 2&3, Indian Institute of Foreign Trade, New Delhi, pp. 70-90.

THE article says that the ASEAN region has emerged as one of the most attractive investment destinations in developing world and attracted a disproportionately large amount of FDI particularly during 1987-96. It says, FDI, is not only a source of capital funds and foreign exchange, but also a dynamic and efficient vehicle to secure the much needed industrial technology, managerial expertise and marketing knowledge employment, productivity and export performance.

Further, it says that India is a sectoral dialogue partner of ASEAN and is actively engaged in the areas of trade, investment, tourism and technology. The economic and trade relations between India and ASEAN have grown rapidly since the late 1970s. ASEAN countries enjoyed high economic growth during this period. FDI contributed substantially to promote investment and employment generation, raising productivity and skill development and export performance in the ASEAN countries.

Flows of FDI, it says, are not very high in India as compared to China and ASEAN. In India, 60 per cent of the total FDI have been in the priority sector and only 6 per cent in the consumer goods sector. In ASEAN countries, FDI has increased in large proportion during the period 1985-96. The ratio of FDI to gross fixed capital formation is as high as 20 per cent. FDI has promoted exports of manufactured goods and there is a large inflow of FDI in trade and commerce. Joint ventures between India and ASEAN have gone up during the last decade. Out of the total Indian joint ventures abroad in 1996, 42 per cent were based in the ASEAN. In terms of equity participation, nearly 55 per cent of the total equity of all the Indian joint ventures were held in industrial ventures in ASEAN. In addition to the industrial joint ventures, Indian entrepreneurs from the private sector have also set up joint ventures in services sector in the areas of construction, consultancy, leasing and trading in the ASEAN region. India can improve its economic relations with ASEAN through FDI and joint ventures.

**Foreign Direct Investment: Trends, TRIMs and WTO Negotiations** by Douglas H. Brooks, Emma Xiaoqin Fan, and Lea R. Sumulong, *Asian Development Review*, Vol. 20, No. 1, 2003, Asian Development Bank, pp. 1-33.

THE article makes a review of the recent developments relating to FDI flows and their impacts on Asian countries. FDI restrictions in these countries, it says, have been dramatically reduced as a result of a host of factors, viz. emergence of globally integrated production and marketing networks, bilateral investment treaties, and opening of their economies by the developing countries to FDI. In addition, the drying up of lending by the commercial banks due to debt crises, many developing countries introduced reforms in their investment policies to attract FDI as the same appeared to be an attractive alternative compared to bank loans. In the process, a host of incentives and subsidies were offered, particularly to MNCs, who supported developing countries, industrial policies.

The article further says that flows of FDI have seen a dramatic rise in the last 20 years due to increasing openness of the host economies. The growing internationalization of trade and investment has prompted some countries to call for increased cooperation through the establishment of international rules and commitments under the World Trade Organization (WTO).

The article has been organized in five sections. Section I reviews the recent developments in FDI flows and their impact on developing countries in Asia. Section II discusses importance of the policy dimensions relating to FDI. Section III explains advantages and disadvantages of FDI. Section IV elaborates on policy options for developing Asian economies pertaining to FDI. The concluding section summarizes the main conclusions and findings.

**FDI and Development: Policy Issues Related to the Growth of FDI in Services,** UNCTAD, TD/B/COM.2/55, 24 November 2003, Geneva.

THE article provides an analysis of the changing sectoral composition of FDI and implications of the increased role of trade in services. It mainly deals with FDI related to privatization of services and FDI for exports. Access to efficient and high quality services, it says, has become increasingly important for the productivity and competitiveness of firms and industries. In an increasingly knowledge-based world economy, access to competitive services in key areas is a pre-condition for developing the supply capacity. Developing countries need to take advantage of trade liberalization and to integrate into the international production system involving both goods and services. Recent developments have opened new opportunities for developing countries to benefit from globalization.

Finally, the article says that services are important as intermediate inputs as well as exported products. Services, as intermediate inputs to the production of goods and services, make an impact on competitiveness in domestic and international markets. Poorly developed service industries can be a major barrier to build up internationally competitive productive capacity. Power failures, breakdowns of telecommunication networks, inefficient transportation systems, lack of an adequate financial infrastructure constitute the other factors which hamper the development of domestic enterprise capabilities as well as the scope of FDI in productive industries. In its concluding remark, it says that services can have an increasingly important direct impact on a country's export performance.

**Should Press Note 18 Be Scrapped?** By S.K. Munjal and Hitesh Gajaria, *The Economic Times*, New Delhi, 27 September 2004, p. 4.

IN a face-off debate on Press Note 18, the two industrialists express their expert views on Press Note 18.

The Confederation of Indian Industry (CII) represents much needed financial resources combined with new technology and modern management, which is necessary for the Indian economy to achieve a GDP growth of 8 per cent and more, says S.K. Munjal, President, CII. He says in the debate that FDI contributes to an improvement in overall competitiveness of the economy and facilitates its effective integration with global trade, technology and financial flows. The Press Note 18 has been a subject of debate and that some foreign investors have expressed their opposition to it. The author is of the opinion that in the specific Indian circumstances, Press Note 18 has served and continues to serve a useful purpose. He believes that the Note has helped and brought a degree of stability and predictability in the establishment and working of joint ventures in the country and has ensured that the legitimate interest of domestic industry, small shareholders, and banks and FIs are protected. The Press Note has generally not come in the way of foreign companies seeking new alliances once there existing ventures have been amicably dissolved.

S.K. Munjal suggests that legitimate needs of foreign investors have to be fully protected and promoted to encourage further FDI inflows into India. Necessary safeguards must be made to avoid any instances of domestic partners taking unfair advantage of Press Note 18 and harassing foreign collaborators.

The Press Note 18 requires foreign investors/ suppliers of technology to seek prior approval from the Government, justifying the need to set up a new joint venture/wholly-owned subsidiary/a new technology transfer (including trade mark) arrangements, if they already have existing tie-ups in the same or allied field with Indian partners. The proposal should not jeopardize the interest of the existing Indian joint venture/technology/trade-mark partners. Operationally, the Government approves such proposals after obtaining a No Objection Certificate from the Indian joint venture partner.

In this context, Hitesh Gazaria, President of Bharat S. Raut & Co., says that the Note is a hurdle in India's otherwise very liberal FDI policy, depicting us as unconvinced liberalizers. It goes against India's obligations under the WTO regime by creating an entry barrier applied selectively against early entrants in the Indian industry.

The Press Note's utility should be contrasted with India's caring need for greater FDI. Scrapping the Note, the author says, could be a turning point in making India one of the most attractive FDI destinations. By now, Indian entrepreneurs have demonstrated convincingly that they can be world champions.

Hitesh Gajaria suggests that the Government would, therefore, do India and its entrepreneurs a world of good by scrapping the Note and encouraging joint venture partners to seek redressal of their grievances through competent contractual arrangements.

**Multilateral Rules on FDI: Do We Need Them? Will We Get Them? A Developing Country Perspective** by Stephen Young and Ana Teresa Tavares, *Transnational Corporations*, Vol. 13, No. 1, April 2004, United Nations, UNCTAD Division on Investment, Technology and Enterprise Development, Geneva.

THE article provides a review and evaluation of multilateral rule on FDI with special reference to implications for developing countries. It examines various issues, viz. Where are we now with multilateral investment rules? Is a multilateral investment regime at the WTO desirable? Are multilateral investment rules actually achievable? Where do we go from here, and what are the implications for developing economies? These issues are the subject of debate. The article also makes an attempt to assist developing countries in deciding their policy priorities. The policy focus for these countries should be on domestic regulatory and institutional reforms, keeping commitment to the multilateral trading system, and the potential benefits from a multilateral investment accord in the longterm.

**Foreign Direct Investment in the Post Globalized Era: India's Strategy and Prospects** By Nawal Kishor, *Business Perspectives*, Birla Institute of Management Technology, Vol. 5, No. 2, July-December 2003, New Delhi.

THE publication says that FDI is considered an important tool for developing countries to push up their economic growth. However, major share of inflows and outflows of FDI are accounted for by the developed countries. India's share in the world FDI inflows was merely 0.5 per cent in 2001. The article makes an analysis of the trends of global FDI inflows in relation to India and some other countries. It makes some suggestions to enhance FDI inflows into India. These include: (i) sectoral FDI caps should be reduced to the minimum and entry barriers eliminated; (ii) the existing strategy for attracting FDI should be overhauled. The relative emphasis must shift from a broad approach to one of targeting the specific companies in specific sectors; (iii) the special economic zones (SEZs) should be developed as the most competitive destination for export related FDI in the world, and (iv) domestic policy reforms in the power sector, urban infrastructure and real estate should be expedited to promote private domestic and foreign investment.

The article also makes a reference of a study 'FDI Survey' conducted by FICCI in 2002. The study makes a host of suggestions to attract FDI in India. These include (a) perception-changing and image-building exercises; (b) concrete and tangible steps towards further reforms; (c) boosting investor sentiments and confidence building measures; (d) simplifying procedure; and (e) improving infrastructure facilities.

**FDI and Technology Intensive Exports from India** by S.P. Agarwal, *Technology Exports*, Vol. 5, No. 2, October-December 2002, pp. 1-4.

THIS article discusses FDI and technology exports. India's manufactured exports have been around 75 to 80 per cent, involving generally low technology exports. Technology intensive exports are estimated at about 17 per cent in total exports and high technology exports are estimated around 6 per cent of the manufactured exports as against 17 per cent in China and 35 per cent in USA. It mentions further that India is ranked 14 among the top 20 export winners, for all sectors of technology from 1985-2000, 5th for resource base manufactures, 16th for non-resource base manufactures, 17th for medium technology manufactures and 9th for low technology manufactures. However, India does not appear in the list of top 20 export winners for high technology manufactures. Thus there is a need to enhance India's non-resource based exports and also technology-based exports. The article also describes that various policies of the Government of India indicate that there is generally a lack of synergies among the thrust sectors identified for exports, FDI and Science and Technology development in the country. The thrust sectors identified for FDI are different and mostly related to infrastructure and services. Similarly, the thrust research areas do not seem to have much emphasis on the above sectors. For example, there are insignificant R&D facilities in areas such as telecom, power, food processing, packaging, auto sector including design and engineering, etc. at national level.

The article suggests active investment of export promotion organizations and industrial associations, particularly those concerned with the identified thrust areas for exports and FDI as well as science and technology organizations at state level is not only desirable but also essential for enhancing the effectiveness of FDI and its impact on exports. The technological capabilities and experiences thus built up should enhance our export capabilities in the area of turnkey projects, infrastructure projects, consultancy services and other related areas. It also further suggests that there is need to establish macro-level databases and conduct policy research relating to the impact of FDI, in particular, on technology intensive exports. Various agreements of WTO including those related to TRIMs, TRIPs, GATS, TBT, IT, etc., are also supposed to be aimed at, so as to develop international competitiveness and increasing international trade, including technology transfers. Such efforts or facilities would also be useful for research inputs and information for negotiations in WTO. The WTO Working Group on Investments and Trade seems to have discussed the experiences of various countries, including a report of the World Bank relating to technology transfers associated with investments. The article says the experiences of various countries do not seem to have established conclusive relationship between investment, technology transfers and trade. However, it has been widely established through various studies for different countries that useful research efforts have direct relevance to the technology intensive exports which in turn reflect the international competitiveness of a firm and the country.

**Globalization of Technology: The Role of Foreign Direct Investment** by Taeho Bark and Hwy-Chang Moon, *Asia Pacific Tech Monitor*, January-February 2002, pp. 20-25.

GIVING a brief background on globalization of technologies and the role of FDI, the article says that FDI has been successfully adopted worldwide to catalyze transfer of globalization of technologies. It is largely effected by multinational firms through their transnational activities, which include investments, joint ventures, licensing, etc. But a firm's ability to catalyze globalization of its technology through FDI channels depends on many competitive factors. In this context this article discusses role of FDI as an instrument to bring about globalization of technologies for the benefit of small and medium enterprises. This article examines, that globalization of technologies through FDI affects the competitiveness of foreign firms and host economies. Some specific policy suggestions are mentioned highlighting some more fundamental policy implications for both foreign investors and host economies.

**FDI: Left Alone – The Debate and the Dilemmas,** *The Economic Times*, 1 October 2004, p. 10.

THIS Article discusses the important areas of FDI like telecommunication, insurance, civil aviation and retailers. On telecom area it says that an increase in the FDI limit will ease the way for a few telecom IPOs. The main beneficiaries of a hike in the FDI cap to 74 per cent will be companies like Bharti, Hutch and Idea, which have substantial overseas holdings and those opposed are fully Indian owned entities like Reliance and TATA. FDI might be a critical issue for some of the mid-sized and smaller companies for whom raising capital is difficult.

The telecom sector, that has been one of the highest FDI flows into the country, is expected to have 100 million subscribers by next year. The argument in favour of increasing the FDI cap for the sector is based on the requirements of around Rs 50,000 crore in next three years to meet the growing needs. These kinds of funds do not exist in the domestic markets.

On insurance, this article highlights the significance of raising the cap from 26 per cent to 49 per cent, which would signal the first move towards further opening up of this sector and should lead to raising it further up to 51 per cent and 74 per cent sooner than expected. It is a known fact that insurance, especially life insurance, is a capital operation.

On civil aviation, the feature says FDI has been restrictive as compared to most other sectors. Although FDI in airlines is allowed up to 40 per cent but foreign carriers cannot invest. In the 2004-05 Budget the Government proposed increase in the FDI limit to 49 per cent. However, the Civil Aviation Ministry is opposed to foreign airlines investing in Indian airlines companies. Simply increasing the FDI cap to 49 per cent does not mean anything unless foreign airlines are allowed to invest. There is an urgent need to bring in a clear policy on FDI in civil aviation.

On FDI in retailing, this feature discusses various pros and cons of this area. It says that FDI in retail is not a priority of the Government. FDI should first be encouraged in technology, infrastructure and manufacturing. Retail is one of the few sectors closed to FDI, primarily due to opposition from the local traders who have been alleging that a large number of jobs generated by small outlets would banish if MNCs enter the fray. There is a rift between the local retail chains, some who want FDI and some who want just protection from the Government.

**Press Note 18: To Withdraw or Not?**
By G. Srinivasan, *The Hindu Business Line*, 4 October 2004, p. 8.

THIS article discusses Press Note 18, which denies automatic route for proposals where financial/technological collaborations between domestic company and its joint venture partner from abroad already exist in the same or allied field. It raises question mark on Press Note 18 of 1998 which remains a road block for FDI and a major hurdle with foreign companies in joint ventures that it needs to be given a quick burial.

When foreign companies used the automatic route of approval for setting up competiting ventures to the detriment of existing collaborations informal representation were made to the Government that foreign collaborators were arm twisting Indian partners to sell their stake in joint ventures on the pain of denying technology support or extending the agreements.

Thus this Press Note 18 was issued on 14 December 1998, on the recommendation of the core group of the Foreign Investment Promotion Board.

Under this rule foreign financial/technical collaborators with joint ventures/technology transfer/trademark agreements in India are required to obtain the nod of the FIPB/Project Approval Board providing justification for the proposed activity and proving that the new proposal would in no way affect the interest of the existing joint venture or technology/trade mark partner.

Press Note 18, which does not cover the information technology sector, international financial institutions and the mining sector (application of this rule is restricted to the same area and or the particular mineral) has served the nation well.

# Report (2003) of the Committee on Trade-Related Investment Measures

**I. General**

1. This report is submitted pursuant to Article 7.3 of the Agreement on Trade-Related Investment Measures, which requires the Committee on Trade-Related Investment Measures to report annually to the Council for Trade in Goods. The Report covers the period October 2002–October 2003.[1]

2. The Committee met on 19 June 2003 under the chairmanship of Mr. Vassili Notis (Greece), and on 18 July and 3 October 2003 under the chairmanship of Mr. Sivaramen Palayathan (Mauritius). Minutes of the meetings are contained in documents G/TRIMS/M/16, G/TRIMS/M/17 and G/TRIMS/M/18, respectively. The meetings were open to Members, governments with observer status in the WTO and international intergovernmental organizations to which the Committee has accorded regular observer status (IMF, OECD, UN, UNCTAD and World Bank). Decisions on requests for observer status from several other international organizations are pending.

**II. Notifications**

3. Article 5.1 of the Agreement on Trade-Related Investment Measures requires Members to notify any trade-related investment measure ("TRIM") inconsistent with the Agreement within 90 days after the entry into force of the WTO Agreement. Article 5.2 of the Agreement gives the benefit of transition periods for the elimination of measures notified under Article 5.1 and which were in existence at least 180 days preceding the entry into force of the WTO Agreement. Pursuant to a decision adopted by the General Council in April 1995, governments eligible to become original WTO Members that accepted the WTO Agreement after 1 January 1995 had a period of 90 days after the date of their acceptance of the WTO Agreement to make the notifications foreseen in Article 5.1, with the period for the elimination of TRIMs notified under Article 5.1 being governed by reference to the date of entry into force of the WTO Agreement itself.[2]

4. Article 5.5 deals with the conditions under which, during the transition periods stipulated in Article 5.2, Members may apply TRIMs notified under Article 5.1 to new investments. While a standard format for the submission of notifications under this provision has been adopted by the Committee (G/TRIMS/3), no such notifications have been made.

5. A number of Members have submitted notifications as required under Article 6.2, which provides for notification to the Secretariat of publications in which information on TRIMs can be found. A list of these notifications has been circulated in G/TRIMS/N/2/Rev.11, dated 24 September 2003. Annex 3 lists the Members which have submitted such notifications.

**III. Special and Differential Treatment Proposals Related to the TRIMs Agreement**

6. In the context of the Work Programme on Special and Differential Treatment (S&D) under Paragraph 44 of the Doha Ministerial Declaration and Paragraph 12.1 of the Decision on Implementation-Related Issues and Concerns, on 20 May 2003 the Chairman of the General Council instructed the TRIMs Committee to consider two S&D proposals related to the TRIMs Agreement. The proposals were submitted by the African Group in document TN/CTD/W/3/Rev.2 with respect to Article 4 and Article 5.3 of the TRIMs Agreement.

7. At its meetings on 19 June and 18 July, the TRIMs Committee held substantive discussions on the proposals. In addition, an informal meeting on 12 June and several informal consultations were held on this issue. A full account of the discussions is contained in the relevant sections of the minutes of the TRIMs Committee's meeting (G/TRIMS/M/16 and G/TRIMS/M/17). The Committee was unable to arrive at a solution that would enable it to adopt the proposals or alternative compromise solutions. At its meeting on 18 July 2003, the Committee agreed on a short written report to be submitted by the Chairman of the TRIMs Committee to the General Council. The report has been circulated as document G/L/638.

**IV. Transitional Review Mechanism Pursuant to Paragraph 18 of the Protocol of Accession of the People's Republic of China**

8. Pursuant to paragraph 18 of China's Protocol of Accession, the TRIMs Committee undertook the second annual review of China's implementation of its commitments under the TRIMs Agreement and related provisions of the Protocol of Accession. Comments and questions in connection with China's Transitional Review Mechanism were received from the European Communities (G/TRIMS/W/31) and the United States (G/TRIMS/W/32). China submitted information on Annex 1A of its Protocol of Accession in the context of the Transitional Review Mechanism. This submission was circulated as document G/TRIMS/W/34, dated 2 October 2003.

9. The review took place at the meeting of 3 October 2003. A full account of the discussions is contained in the minutes of the meeting (G/TRIMS/M/18). The Committee adopted *ad referendum* a Report of the Chairman on the results of the review. The report was forwarded to the Council for Trade in Goods as document G/L/648.

[1] The previous annual report is contained in document G/L/589 of 8 November 2002.

[2] WT/L/64.

## COUNCIL FOR TRADE IN GOODS

### Committee on Trade-Related Investment Measures

# The Mandated Review of the TRIMs Agreement Paragraph 12(b) of the Doha Ministerial Declaration Implementation-related Issues and Concerns (tiret 40)

COMMUNICATION FROM BRAZIL AND INDIA

The following communication, dated 8 October 2002, has been received from the delegations of Brazil and India, with the request that it be circulated to the Council for Trade in Goods and to the Committee on Trade-Related Investment Measures.

**I. Background**

1. The TRIMs Agreement has established in Article 9 a comprehensive provision on its own review, which includes the possibility of Members proposing amendments to its text. This provision stemmed from the understanding of many Members at the end of the Uruguay Round (UR) – especially developing countries – that the scope of the agreement had gone beyond the mandate agreed to in the Punta del Este Declaration. That mandate stated that "following an examination of the operation of GATT Articles related to the trade-restrictive and distorting effects of investment measures, negotiations should elaborate, as appropriate, further provisions that may be necessary to avoid such adverse effects on trade". However, instead of addressing directly such alleged adverse effects on trade, the TRIMs Agreement simply prohibits some investment measures presumed to be inconsistent with Articles III and XI of GATT 1994.

2. Furthermore, paragraph 12 of the Doha Ministerial Declaration determined that negotiations on outstanding implementation issues shall be an integral part of the Work Programme. Pursuant to item "b" of that same paragraph, these issues include those set out in tirets 37 to 40 of document Job(01)152/Rev.1, which are directly related to the TRIMs Agreement. This paper refers to issues related to tiret 40.

3. Since the end of the UR, the argument against the use of investment measures has lost much of its theoretical strength. New developments in the theory of international trade have raised doubts with respect to models of perfect competition, that have become increasingly seen as unrealistic or based on questionable assumptions. Furthermore, the argument according to which resort to these measures inevitably results in trade distortions has not been proved by empirical evidence.

4. A recent joint study by the WTO and UNCTAD Secretariats (G/C/W/307) is relevant in this regard. If it is true that this study does not add up to a decisive argument in favour of local content, trade balancing, and export performance requirements, it does, however, weigh against any kind of general assumption that such measures necessarily distort trade. Moreover, history provides many examples of successful recourse to investment measures to address developmental objectives as well as to offset trade-distorting effects of certain forms of corporate behaviour - which in the case of developing countries may affect the efficient allocation of resources in a more negative way than investment measures. In addition, it must be pointed out that other currently WTO-compatible measures have revealed themselves to have a much more distorting effect on international trade, particularly in sectors of export interest to developing countries, than those related to investment.

5. One issue of extreme importance for developing countries is technology. The gap between developed and developing countries in terms of technology tends to grow over time, as the international economy moves from the traditional factors of production into a paradigm of production reliant on technology, knowledge and innovation. Trade-related investment measures in the area of science and technology are necessary in order for these

countries to increase their share in the higher-technology segment of international trade and to avoid what would inevitably be a decline of their participation in world trade as a whole as high-technology goods become the only dynamic sectors.

6. Competition policy is another area of interest. New evidence shows that trade-related investment measures can, if properly implemented, generate benefits to the competitiveness environment. Over the last two decades, a massive expansion of corporate power took place in developed and developing countries. The risks of excessive corporate power can be reduced through incentives to other investors to compete in the domestic market.

7. Trade-related investment measures can also be valuable instruments of regional development policies. There are circumstances in which goods originating from disadvantaged regions of developing countries cannot compete in the short term with goods produced by more advanced methods or technologies. Since it does not make economic sense for the State to support these regions indefinitely, trade-related investment measures associated with purchases from companies located in those disadvantaged regions can provide an additional stimulus for such companies to grow and improve their ability to compete.

8. Trade-related investment measures can also be positively associated with sustainable development as they relate to environment concerns. Unlike developed economies, developing countries do not have all the means to ensure environment protection and therefore need to generate additional income to that effect. It is widely recognized that certain natural resources and regions are best protected in developing countries when sustainable management policies are implemented with focus on specific products. It is therefore necessary to promote environment-friendly processes and goods, in most cases under conditions which may not be competitive. Such processes and goods may only find their way into the market by means of an induced demand which, in turn, could be generated through trade-related investment measures.

9. One additional and special concern for developing countries lies in the fact that external financial weaknesses are sometimes structural and, as such, become a major risk for the stability of trade flows. Developing countries have been seriously affected by the financial turbulence of the past five years, as they face structural imbalances in their external sectors, which can only be eliminated in the development process over time. Usually, developing countries must generate trade surpluses if they are to maintain a normal flow of transfers and payments, even if they are not faced with an acute balance of payments crisis. There are two ways of generating trade surpluses, namely export increases and import reductions, but only the former brings benefits for the multilateral trading system. When faced with structural imbalances in the external front, developing countries should be encouraged to increase exports in order not to restrict imports with deflationary policies. Trade-related investment measures related to exports can be less restrictive than deflationary policies for a country's external trade flows and for the multilateral trading system as a whole.

10. The disciplines of the TRIMs Agreement disregard the above structural inequalities among Members and, apart from already concluded transitional periods, incorporate no specific meaningful clauses for special and differential treatment. The absence of effective and operative clauses aiming at addressing the special needs of developing countries has made the TRIMs Agreement one example of reverse special and differential treatment. While developed countries had decades to choose when, how and in which economic sectors to apply such measures, developing countries had their right to choose simply revoked. Besides, the provisions of Article 4, as they are confined to the exceptions permitted in Article XVIII of GATT 1994, in the Understanding on the Balance-of-Payments Provisions of GATT 1994, and in the Declaration on Trade Measures Taken for Balance-of-Payments Purposes adopted on 28 November 1979, are clearly insufficient in providing the necessary flexibility to make use of investment measures in the context of development policies. Furthermore, these exceptions are indicative that the GATT recognizes that quantitative restrictions allow developing countries to conserve their foreign currency assets for purchases of imports needed for development.

*(Conted on p. 44 )*

## Committee on Trade-Related Investment Measures

# Transitional Review Mechanism Pursuant to Paragraph 18 of the Protocol on the Accession of the People's Republic of China ("China")

Information to be Notified to the Committee on Trade-Related Investment Measures as Required in Annex 1A to the Protocol of Accession of the People's Republic of China

COMMUNICATION FROM CHINA

The following communication, dated 1 October 2003, has been received from the Permanent Mission of the People's Republic of China.

**I Investment Regime**

*(a) Completed revisions to investment guidelines in conformity with the WTO Agreement*

China has revised the Guiding Industrial Catalogue for Foreign Investment in line with the WTO Agreement in the year of 2002. Relevant information has been provided last year which was contained in the document G/TRIMS/W/26.

**II. Trade-Related Investment Measures**

*(a) Elimination and cessation of enforcement of trade and foreign exchange balancing requirements, local content and export performance offsets and technology transfer requirements made effective through laws, regulations or other measures*

Before accession to the WTO, China had already modified three basic laws in respect of foreign direct investment – Law of People's Republic of China on Sino-Foreign Equity Joint Ventures, Law of People's Republic of China on Sino-Foreign Cooperative Joint Ventures and Law of People's Republic of China on Foreign-invested Enterprises as well as their implementing rules. The revised legislation has eliminated or ceased the implementation of provisions on foreign currency balancing, local content, export performance requirement and mandatory technology transfer.

*(b) Amendments to ensure lifting of all measures applicable to motor vehicle producers restricting the categories, types or models of vehicles permitted for production (to be completely removed two years after accession)*

According to Paragraph 205 of the Working Party Report on the Accession of China, the category authorizations by the Chinese Government could continue to distinguish between trucks and buses, light commercial vehicles and passenger cars. In the Policy on the Development of Automobile Industry, which is in the process of revision, the measures restricting the production under each category will be eliminated. The new Policy is now waiting for the approval from the State Council and will be enforced as soon as the legislative procedures are completed.

*(c) Increased limits within which investments in motor vehicle manufacturing could be approved at the provincial government at the levels outlined in the Report*

The draft of the upcoming development policy on automobile industry is characterized by its provisions on deregulation and transfer of approval authority to governments at provincial levels. After the issuance of the new Policy, the invest limits on auto manufacturing that could be approved at provincial level will be increased as required in the Working Party Report.

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## Committee on Trade-Related Investment Measures

# Transitional Review Mechanism Pursuant to Paragraph 18 of the Protocol on the Accession of the People's Republic of China ("China")

COMMUNICATION FROM THE EUROPEAN COMMUNITY
AND ITS MEMBER STATES

The following communication, dated 14 August 2003, has been received from the Permanent Delegation of the European Commission.

I. **General**

1. In connection with its accession to the WTO, China assumed a number of commitments with respect to existing WTO agreements and the obligations contained therein.

2. A number of these commitments relate to the WTO Agreement on Trade-Related Investment Measures ("TRIMs") and are reflected primarily in paragraph 18 of the Chinese Protocol on Accession which also establishes a transitional review mechanism ("TRM") providing for the General Council to review China's implementation of the WTO Agreement within one year after accession.

3. On TRIMs, has China committed itself to comply fully with the TRIMs Agreement through abolishing legislation and other measures constituting TRIMs upon joining the WTO and through "providing relevant information, including information contained in Annex 1A, to each subsidiary body in advance of the review". More specifically, paragraph 3 of the Accession Protocol for China reads:

> "3. China shall, upon accession, comply with the TRIMs Agreement, without recourse to the provisions of Article 5 of the TRIMs Agreement. China shall eliminate and cease to enforce trade and foreign exchange balancing requirements, local content and export or performance requirements made effective through laws, regulations or other measures. Moreover, China will not enforce provisions of contracts imposing such requirements. Without prejudice to the relevant provisions of this Protocol, China shall ensure that the distribution of import licences, quotas, tariff-rate quotas, or any other means of approval for importation, the right of importation or investment by national and sub-national authorities, is not conditioned on: whether competing domestic suppliers of such products exist; or performance requirements of any kind, such as local content, offsets, the transfer of technology, export performance or the conduct of research and development in China."

II. **Chinese TRIMs – Request for Further Clarification**

4. In response to the questions posed by the European Community and its Member States (the "EC") in submission G/TRIMS/W/21, as well as questions posed by other WTO Members regarding modifications to its TRIMs, China issued Communication G/TRIMS/W/26. In addition to this document, the Head of the Chinese Delegation delivered a detailed and informative statement dated 14 October 2002 during the 14 October 2002 meeting of the TRIMs Committee. That statement provided further clarification concerning certain questions raised by other WTO Members.

5. Having carefully analyzed the document and the statement in question, the EC would be grateful for some additional clarification on a number of points. This would allow the EC to gain a better understanding of and assess more fully the progress made by China in abolishing or modifying its TRIMs and TRIMs incompatible legislation as required.

*Question 1*

Upon acceding to the WTO, China accepted to provide information regarding a number of economic policy areas (as well as other areas).

In the area of investment specifically, China accepted to provide the Committee on Trade-Related Investment Measures with information about "completed revisions to investment guidelines in conformity with the WTO Agreement", cf.. Annex 1A, II, 2 (paragraph 85) of document WT/ACC/CHN/49.

*Can China confirm that such revisions have in fact taken place, and, what the revisions consist of more precisely, especially as regards the status of the Catalogue on Investment and the categorization of restricted; permitted; and encouraged investments, and requirements relating to transfer of technology?*

*Question 2*

The above-quoted paragraph 3 of the Accession Protocol for China lays out a clear obligation for China to not only abolish or amend TRIMs-incompatible legislation, but also to ensure that any contracts containing TRIMs incompatible commitments and obligations would not be enforced.

However, the EC notes that – according to the Chinese answers so far provided - obligations contained in *existing* contractual arrangements will nevertheless remain valid and enforceable even where such arrangements contain TRIMs-incompatible commitments.

During the last TRM regarding TRIMs China stated its respect for the freedom of parties to enter into contracts and added that commitments entered into by (foreign) producers continue to be enforceable, as "such commitments cannot be deemed invalid … [and] the enterprise shall continue to honour its commitment made in the contract" and the fact that in relation to foreign investment, the contracts and articles of association of a foreign invested enterprise become effective only after they have been approved by the competent authority.

That answer would appear to be in direct contradiction with the explicit undertaking under paragraph 3 of the protocol to ensure that contracts which contain TRIMs-incompatible commitments and obligations are no longer enforceable.

*Can China confirm that contractual arrangements which contain TRIMs-incompatible commitments and obligations should be amended in such a way that they will contain obligations which are fully compatible with the TRIMs Agreement?*

*Can China indicate how such amendments might be instituted, including through a renegotiation of the relevant parts of a contract?*

*Can China confirm that for its part it will ensure that any contracts which may contain TRIMs-incompatible commitments and obligations will not be enforced before domestic law courts or other administrative tribunals or bodies and that the TRIMs-incompatible commitments and obligations are to be considered null and void?*

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(Conted from p. 41 )

**II. Proposal**

11. Article 4 of the TRIMs Agreement should be amended in order to incorporate specific provisions that will provide developing countries with the necessary flexibility to implement development policies. One possible solution is to extend the range of situations in which developing countries are allowed to deviate temporarily from the provisions of Article 2. Among the new provisions that should be included, the following should be considered.

12. Developing countries should be allowed to use TRIMs in order to:

(a) promote domestic manufacturing capabilities in high value-added sectors or technology-intensive sectors;

(b) stimulate the transfer or indigenous development of technology;

(c) promote domestic competition and/or correct restrictive business practices;

(d) promote purchases from disadvantaged regions in order to reduce regional disparities within their territories;

(e) stimulate environment-friendly methods or products and contribute to sustainable development;

(f) increase export capacity in cases where structural current account deficits would cause or threaten to cause a major reduction in imports.

(g) promote small and medium-sized enterprises as they contribute to employment generation.

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