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PARADIGMS OF FDI STRATEGIES IN INDIA AND CHINA

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INTRODUCTION

The Asian Dragon and Elephant have been treated as competitors while both the economies are complementary to each other. Both have taken different routes to enter the world economy and that has resulted in their joining complementary strengths. As both get to grips with their respective problems- economic development, each seemingly a mirror image of the other, it appears inevitable that convergence of each country's economic development model will lead to increased competition. Thus, it goes without saying that China and India have developed differently; this has been illustrated in the following Exhibit 1.

Exhibit.1: Foundations

	China	India
Government	Single party rule, Decision making regarding FDI by both Central and Provincial Government independently	Coalition Government, Decision making regarding FDI by only Central Government.
Information and Transparency	Only Partial Economic Information availability	Full Economic Information availability
Property Rights	Private rights sacrificed for Government interest	Government rights sacrificed for Private interest

COMPARATIVE VIEW POINTS

A. FDI CONCEPTS:

According to IMF definition, under international norms, 14 different items are included under the broad rubric of equity capital, reinvested earnings and other capital. But six of them do not form part of FDI concept in India. In contrast, China adheres to the IMF standard of FDI computing. China includes all the components of IMF in its definition of FDI. It also classifies imported equipment as FDI, while India captures these as imports in its trade data. China's FDI numbers also include a substantial amount of round-tripping. The differences in the constituent elements of FDI are shown in Exhibit A.1 in appendix.

FDI inflows in India are entirely measured on equity investments hence FDI inflows into India have been underestimated. FDI gap between India and China is not nearly as huge as figures shows.

There are two dimensions of the huge reported discrepancy between the FDI inflows of India and China:-

(i). Over-reporting of FDI by China in terms of its alleged 'round-tripping'.
(ii). Under reporting of FDI by India because of non-conformity of India's method of measuring FDI to the international standards (Pfeffermann).

With uniformity in the FDI measuring standard of the two countries in line with the international norm and with appropriate adjustment for round-tripping in case of China, the difference in terms of ratio of adjusted FDI to GDP between India and China could become much smaller.

The Chinese reforms have been much more wider and deeper than India's and Chinese provinces have been competing much more among themselves to attract FDI relative to the Indian states. China liberalised its trade and investment regime a decade before India did.

B. FDI STRATEGIES

I. *Investment and Business Scenario :*

The Chinese Strategy: A pre-condition to FDI inflows is the creation and sustenance of a well-designed business environment or 'investment climate' for the benefits of FDI to be realised by a developing economy (Fields and Pfeffermann, 2003). China is today the 2nd largest FDI destination. But the paradox is that its investment climate is not liberal in all directions. China's FDI policy is still relatively restricted in terms of FDI forms, foreign

ownership shares, access to certain activities and performance requirements. China's laws and regulations unambiguously stipulate that Foreign Invested Enterprises (FIEs) can choose from among three different forms to invest in China contractual joint ventures(CJV); equity joint ventures(EJV); and wholly foreign-owned enterprises (WFOE).

Table -1: Different Forms of Foreign Invested Enterprises (FIEs)

CJV	EJV	WFOE
➢ There is no minimum foreign contribution required to initiate a cooperative venture. ➢ The contributions made by the investors are not required to be expressed in a monetary value. ➢ The foreign investor is permitted to withdraw their registered capital or a portion thereof from the cooperative venture during the duration of the cooperative venture contract.	➢ Share holdings in a joint venture are usually non-negotiable and cannot be transferred without approval from the Chinese government. ➢ Investors are restricted from withdrawing registered capital during the live of the joint venture contract. ➢ A minimum of 25% of the capital must be contributed by the foreign partner(s). There is no minimum investment for the Chinese partner(s).	➢ There are several pre-establishment considerations that investors should take into account before committing to the WFOE as an investment vehicle in China. ➢ # Liberalized Capital Requirement ➢ ## Business Scope to be written and approved. ➢ ### Additional Tax Benefits
#, ##, ### - Please refer Appendix		

i. Relaxations: The new Catalogue eases the norms by removing various Special administrative measures, as follows-

a) Manufacturing Sector –

- ➢ Manufacturing of high energy power batteries for new energy automobiles
- ➢ Design and manufacturing of civil satellites, manufacturing of civil satellite payload
- ➢ R&D and manufacturing of automobile electronic network and electronic controllers for electric power steering systems

- Manufacturing of rail transport equipment
- Manufacturing of liquid biofuel (fuel ethanol, biofuel)
- Manufacturing of motorcycles
- Manufacturing and repair of marine engineering equipment (including modules)
- Processing of edible oil and fats from soyabean, rapeseed, peanut, cottonseed, camellia seed, sunflower seed, and palm
- Processing of rice, flour, and crude sugar, and deep processing of corn
- Manufacturing of low and medium-speed diesel engine and crankshafts for vessels
- Manufacturing of blade electric vehicles (BEVs)

b) Service Sector –

- Operation of accounting and auditing services
- Operation of highway passenger transport services
- Operation of ocean shipping tally companies
- Operation of credit investigation and rating services
- Construction and operation of large-scale agricultural product wholesale markets
- Establishment and operation of water conservancy projects

c) Mining Sector –

- Exploration and development of oil shale, oil sands, shale gas, and other unconventional oil and gas
- Exploration and mining of precious metals (gold, silver, platinum)
- Lithium mining and mineral processing
- Smelting of rare metals, including tungsten, molybdenum, tin (excluding tin compounds), and antimony (including antimony oxides and antimony sulphides)

ii. The Encouragement: The Catalogue adds six new industries to the encouraged category:-

- Manufacturing of intelligent emergency medical rescue devices
- R&D and manufacturing of virtual reality (VR) and augmented reality (AR) devices
- Establishment and operation of city parking facilities
- Development and manufacturing of key components for 3D printing devices
- Construction of hydrogen refueling stations

- Manufacturing of hydrographic monitoring sensors

iii. The Prohibitions:

- While the Catalogue relaxes restrictions in a variety of industries, general aviation – including common airlines for agricultural, forestry, and fishing – and banking face tighter regulation with the update. Additionally, the following industries now fall under the "prohibited" category:
- Aerial photography mapping
- Editing and publishing of books, newspapers, and periodicals
- Editing, publishing, and production of audio-visual products and electronic publications
- Radio, television video-on-demand businesses, and satellite television broadcasters receiving facility installation services
- Internet public information services
- Research institutes of humanities and social sciences

iv. The IPR Protection

- IPR Protection available in China as per 'first-to-file' policy, which may pose a problem for foreign companies, who are willing to expand their brand in China, as there is possibility that the IPR has already been filed by an opportunistic investor.
- In addition to securing their IPR, companies must then be proactive and vigilant about protecting it. Many companies do regular online research, as well as attend trade shows and other functions, to check for possible violations. Companies can also request that Chinese customs monitor for trademark infringement, free-of-charge (at the time of writing).

Some general measures that companies should take to protect their IPR:

- **Copyrights**: register works with the National Copyright Administration to ensure evidence of ownership;
- **Patents**: follows 'first-to-file' system and must be filed with the State Intellectual Property Office in Beijing. Those without a commercial office in China must file patent applications through an authorized patent agent;
- **Trademarks**: follows 'first-to-file' system and must be filed with the Trademark Office of the State Administration for Industry and Commerce (SAIC) in Beijing and its 13 local offices. Careful attention

should be paid to the category under which the trademark is filed, as the trademark will be protected only within that category. Foreign companies must file through an authorized trademark agency.

vii. Tax Planning

Lower indirect taxes in China account for almost half of the total price difference, if compared to India.

- Higher labour productivity further decreases prices by 5%, while lower raw material prices in China account for another 4% and lower capital costs for 2.5% of the Indian retail price. The remainder of the price difference of close to 7% of the retail price is the result of such other factors as margins, capital productivity and difference in specifications between the Indian and the Chinese product.
- The study found the average incidence of import duties in China is 17%, and the trade-weighted average about 13% almost half of India trade-weighted level of 24%. Import duties on several key raw materials, such as plastics and aluminum, are much higher in India than in China. Higher import duties on raw materials result in higher prices of inputs, as most domestic players resort to import parity pricing. China has a flat 17% VAT rate (about 14% of the retail price), while India indirect taxes range from 25% to 30% of the retail price for most manufactured products.
- China also provide incentives in various forms to High New Technology Enterprise (HNTE), viz preferential tax rates, 50% or 75% "super deduction" for qualifying R&D expenditure, tax holidays for first 2 years followed by lower interest rates for next 3 years etc..

THE INDIAN STRATEGIES

FDI in India is freely allowed within the ceiling percent of stake, in most of the sectors including service sector under some notified sectoral policy. Therefore, FDI could be brought in India through the automatic route under the power vested with RBI or through Government approvals.

i. Abolition of FIPB on 24.05.2017

Implications:

(i) Formation of Limited Liability Partnerships (LLP) now becomes easier.
(ii) Further flexibility of FDI norms is expected.
(iii) Tedious approval processes and ancillary red-tapism will be eradicated.
(iv) An indication of opening up of strategic sectors.

ii. Startup India

- A startup will mean an entity (private limited company or a registered partnership firm or a limited liability partnership) incorporated or registered in India not prior to five years, with an annual turnover not exceeding INR 25 Crores in any preceding financial year, working towards innovation, development, deployment or commercialization of new products, processes or services driven by technology or intellectual property and satisfying certain conditions given in the Regulations.
- Government on16.01.2016 initiated new Policy with various lucrative benefits offered to new investors which are well highlighted in the figure bellow -

Figure - I

Source: - *Start-up India official Web page*

- Government of India has already permitted to invest 100% FDI through Foreign Venture Capital Investor **(FVCI)** to Start-up Investors. RBI eases the norms with following notification –

"Equity or equity linked instrument or debt instrument issued by an Indian 'startup' irrespective of the sector in which the startup is engaged."

i. Sectoral Relaxation of FDI:

➢ **Upto 100% is allowed in the sectors:-**

Agriculture & Animal Husbandry , Plantation Sector, Mining, Mining (Coal & Lignite), Mining, Petroleum & Natural Gas, Defence Manufacturing, Broadcasting, Up-linking of Non-'News & Current Affairs' TV Channels/ Down-linking of TV Channels, Publication of facsimile edition of foreign newspapers Publishing/printing of scientific and technical magazines/specialty journals/

periodicals, subject to compliance with the legal framework as applicable and guidelines issued in this regard from time to time by Ministry of Information and Broadcasting., **Civil Aviation – Airports, Civil Aviation – Air Transport Services, Civil Aviation, Construction Development: Townships, Housing, Built-up Infrastructure, Industrial Parks (new & existing), Satellites- establishment and operation, subject to the sectoral guidelines of Department of Space/ISRO, Telecom Services, Cash & Carry Wholesale Trading, E-commerce activities** (e-commerce entities would engage only in Business to Business (B2B) e-commerce and not in Business to Consumer (B2C) e-commerce.), **Single Brand retail trading, Duty Free Shops, Railway Infrastructure, Asset Reconstruction Companies, Credit Information Companies (CIC), White Label ATM Operations, Financial services activities regulated by RBI, SEBI, IRDA or any other regulator, Food products manufactured or produced in India, Pharmaceuticals(Brown Field), Pharmaceuticals(Green Field),**

- **Upto 74 % in Banking-** Private Sector, Private Security Agencies
- **Upto 51%**Multi Brand Retail Trading
- **Upto 49%** Petroleum & Natural Gas, Broadcasting Content Services, Infrastructure Company in the Securities Market, Insurance, Pension Sector, Power Exchanges
- **Upto 26% in Print Media, upto 20% in Banking-** Public Sector

ii. Tax Planning

- **Reduction in Corporate Tax Rates**

As per the demand from the startup ecosystem for a lower corporate tax rates, the Government has reduced the tax rates to 25%(from the existing 30%) for startups and SMEs whose turnover is not more than 50 crores. This move is in line with international best practices.

The idea is to promote private limited companies, which is a more structured form of business organization. Since, this benefit is available only to domestic companies. Foreign companies (i.e. companies with no Indian subsidiary) and other forms of businesses like LLP and partnership firms are not eligible for this reduced rate.

- **Tax Holidays**

The FM has announced that entities incorporated post 31st March 2016 and approved by Startup India can avail a three-year tax holiday in the first seven years of the business instead of the first five years which were previously provided to them.

- **Implementation of Goods & Service Tax (GST)**

GST is implemented w.e.f. 1st July 2017, it embodies the principle of "one nation one tax' unifying the country into one common market. The five tax categories under GST:0%, 5%, 12%, 18% and 28%.

It will increase the ease of doing business for corporates, reduction in overall taxes for consumers, inflation will come down, tax avoidance difficult, GDP will be benefitted.

- **No capital gains**

Government has exempted conversion of preference shares to equity and otherwise from the definition of 'transfer' giving a relief to startup investors who prefer buying convertible preference share. Preference shares are the most common instruments for foreign investors to invest in India.

iii. Diaspora Attraction :: A Comparison

In order to attract FDI from Chinese diaspora China has started a programme 'Chun Hui' for Non-Resident Chinese (NRC) under this programme for leveraging the diaspora strength in the economy in the form of FDI inflows the Chinese government has given a red carpet treatment to the NRCs in 1991 the percentage of NRC to total FDI of China was about 71.28%. In 1993 this percentage mounted to the highest level of 82.91% later on it has started decreasing due to the heavy influx of non-Chinese FDI. In the year 1977 the aforesaid share came done to 65%. The share of NRC in the recent year have further reduced to less than 50% of the total China's FDI inflows because proportion of non-Chinese FDI has been galloping with high intensity. Overall China's development as a heaven for FDI and a source of labour intensive exports is logical as well as chronological sequel to the pacific miracle, $ 45 mn to $ 50 mn Chinese invest in China 2001. From January to December 2012 the FDI contribution from Hong Kong alone was US$ 111.716 bn which was 64% of the total. The overseas Chinese have a very important role in inward FDI in China. This all is not because NRC's are very patriotic but due to the various departments and efforts of Chinese Government to allure them by offering special privileges.

The reach of Chinese diaspora is the effort of five institutions those are:-

- State Council's Overseas Chinese Affairs Office
- The China Zhigong Party
- The Overseas Chinese Affair Committee Of National People's Congress
- The Hong Cong Macaw Taiwan Compatriots and Overseas Chinese committee of Chinese people's political consultative conference
- All china federation of returned overseas Chinese.

The Institutions attracted with diaspora while operating at different levels from national to local and they all work in tandem with the ministry of foreign affairs and other ministries that are involved to formulate and implement policies, which can attract the diaspora. These three agencies are 'state administration agencies, the important structures of multi-party cooperation and political consultation under the leadership of the CCP, and the people's organizations'.

There is an overseas expert advisory committee of the overseas Chinese affairs office, which has renowned scientists, scholars and entrepreneurs from various countries, they provide policy recommendations and feedback on policy decisions on NRC's.

However, India's development has no such organic link with the East Asian experience. Expatriate Indian entrepreneurs that are Non-Resident Indians (NRIs) played but a minor role in Asia's growth and their investment had a negligible share in India's total FDIs. The role of diaspora is different in China since the government is focused in it as a source of FDI, bringing individuals back to promote Country's development and their diaspora contribution to FDI were 50-70%, for decades. Advantage was because their diaspora is situated in Hong Kong, Taiwan etc., which are geographically close area and Chinese government actively enacted laws and favoured policy to attract them. On contrary, India's diaspora were geographically far apart and there were no special efforts to allure them, resulting their contribution to FDI are meager to the level of 3-4% only, except in 2015, where it scored more. It is because, India's relationship with its diaspora was limited to the soft power and expertise if members remain abroad, till recent. **Now the Government is focusing on NRI's, who can act as informal ambassador** for India in their own country, demonstrating the value of ties with India to Foreign Government.

- **Special Economic Zone (SEZ)/Export Processing Zone (EPZ):**

EPZs are industrial estate while SEZs are industrial township. Both EPZ or other SEZ attract foreign investment and to initiate the process of manufacturing export-led growth. These zones have attempted to carve out a geographical zone in which export-businesses can conduct profitable export-oriented activities, exempt from costly regulations, tax laws, and labor standards that apply more generally within the country.

- **China's Progress –**

In China, major platform for labor-intensive manufacturing exports were the SEZs in which favorable export conditions were assured. The success of Shenzhen and the other Special Economic Zones encouraged the Chinese government to add 14 cities plus Hainan Island to the list of Special Economic Zones in 1986. The urban export-oriented enterprises in China were encouraged by the designation of a growing number of SEZs, coastal 48 open cities and economic and technological development zones, all designed to encourage manufacturing exports. In addition, 15 free-trade zones, 32 state-level economic and technological development zones, and 53 new and high-tech industrial development zones have been established in large and medium-sized cities. All key aspects of the export environment were secured. Exporters, were allowed to import intermediate products and capital goods duty free. They were given generous tax holidays. Exporters were assured decent physical infrastructure, within specially created industrial parks. China has demonstrated through its own experience that creation of SEZs attract substantial FDI for the export sector.

On 31 March 2017, the Chinese State Council approved the launch of seven new FTZs. The new FTZs opened on 1 April 2017, bringing the total number of FTZs to eleven. In contrast to the existing FTZs, which are all located in rich coastal areas, the new FTZs are mainly located in underdeveloped areas in China's interior.

The locational shift indicates two policy considerations. First, the Chinese government is using the new FTZs to stimulate regional economic development and further develop its interior. Second, the location of the new FTZs is designed to contribute to China's national development strategies, most importantly One Belt, One Road ("**OBOR**").

The seven new FTZs and their key areas are as follows:

1. The western FTZs, located in Chongqing, Shaanxi and Sichuan, serve the main purpose of opening up western China for foreign investments through the promotion of comprehensive economic reform. They will be developed as an OBOR transport, logistics and commerce centre (including the port of Guoyan).

The government wants to create a cluster for high-end industries, such as cloud computing and biological medicine in Chongqing.

2. The Hubei and Henan FTZs will mainly serve as focal point of logistics and transportation within the OBOR strategy. The Hubei FTZ will accommodate industrial transfers from the coastal regions to central China, while the Henan FTZ will provide a hub for international cultural trade and medical tourism. _
3. The aim of Liaoning FTZ is to enhance productivity and competitiveness of northeast China's industrial base through economic reforms. To support, the Chinese government aims to develop a modern finance and IT services industry alongside advanced equipment manufacturing, including automobile and aerospace.
4. The Zhejiang FTZ is located in an already economically well-developed area. The focus is on further developing currently existing economic activity, and new focus on exploring the liberalisation of international commodity trading, basically regarding to oil and associated products.

CHINA'S REVISED FTZ NEGATIVE LIST

The new "negative list", On 16 June 2017, it is a list of sectors for which foreign investment in FTZs is subject to specific restrictions, or still completely prohibited. For those industries not mentioned on the list, foreign investors will receive treatment equal to domestic Chinese companies.

The list became effective on 10 July 2017. The new list is narrower than that of 2015: 27 measures in 20 different industries have been removed, including shipbuilding, aeronautical, automotive and railway manufacturing, road and water transportation, and mining. In these industries, specific measures that have been removed are the design and manufacturing of specific helicopters and aircrafts, exploration and mining of certain precious metals, and the construction and operation of large scale theme parks.

Many of the visible liberalised industries feature dominant Chinese companies. Additionally, depending on the industry, foreign investments can still be subject to a MOFCOM filing and national security review, providing the Chinese authorities with a powerful tool for control.

➢ **India's Progress –**

India also had similar models of EPZ and EOU. EPZs are located at various places including Cochin, Falta (near Calcutta), Kandla, Chennai, Noida, Santacruz (Mumbai), Vishakhapatnam and Surat. Incentives provided to attract investment in these areas were 'zero import duty', a 'special 10-year income tax rebate' and other incentives

like 100% FDI in manufacturing sector through automatic route and full freedom for sub contracting from abroad and domestic tariff areas. The government has converted these EPZs into operational SEZs. Eight EPZs in India have contributed a meager Rs 85.52bn in exports (4.3% of country's exports) in 2001.That one of the reason for failure was the poor quality of infrastructure and other facilities is evident from the fact that the government invests only Rs170 mn annually in the seven of the government-owned EOUs.

204 SEZs are operating in India and 18 of these were notified prior to the enactment of SEZ Act (2005). Though SEZs were intended to act as a catalyst for regional development, they are concentrated only in few states (Figure 1). Five states, namely, Andhra Pradesh (AP) (including Telangana), Tamil Nadu (TN), Karnataka, Maharashtra, and Gujarat, have nearly three-fourths (74%) of the operational SEZs, whereas states like Bihar (including Jharkhand), Goa, Delhi and North-eastern States do not have even a single SEZ. Sector-wise, the maximum approvals have been given in the sectors IT/ITes/Electronics industries (comprising 63% of total approvals).

"A processing zone for medicinal plants is proposed to be set up in Chattisgarh and once the pilot project fructifies, the government will replicate the model in other states of Andhra Pradesh, Jammu and Kashmir, Karnataka, Tamil Nadu and Uttarakhand," said Minister of State for Commerce, Government of India at the inauguration of 'Arogya', an international fair on alternative systems of Indian medicines. While the government would provide infrastructure and technical assistance for the zones, investments would come from private entrepreneurs, Ramesh said, adding that the units would cater to both domestic and export markets.

The government of India has approved six proposals from four developers to set up new special economic zones (SEZs) in 2016 across three states in areas such as IT and biotechnology. The decision was taken by the Board of Approval (BoA), headed by Commerce Secretary Rita Teaotia, on November 9th, 2016.

The developers who got nod for new zones include Vaxenic India, EON Kharadi Infrastructure and KRC Infrastructure.

GAR Corporation has proposed to set up two IT/ITeS zones in Telangana, while Vaxenic India wants to set up biotechnology and bio pharmaceuticals SEZ in the state.

EON Kharadi Infrastructure and KRC Infrastructure too have planned to set up separate IT/ITeS special economic zones in Pune. Information Technology Park has got the approval to set up IT zone in Karnataka.

The exports in India by SEZs has increased to 50.5% i.e US$ 65 bn in 2011-12 accounting for 23% of India's export.

- **Financial Asset Management:**

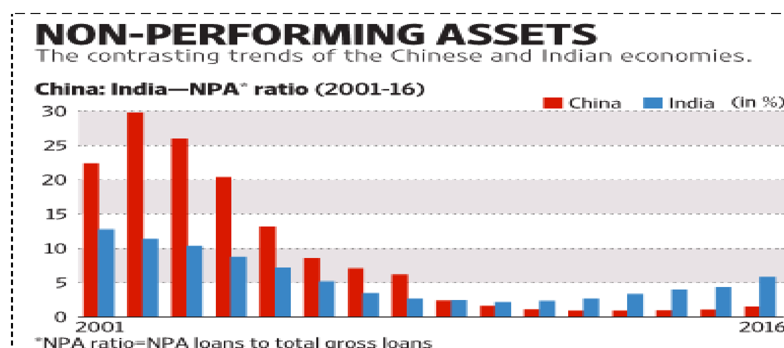
Chinese government had started the liberalization of their loaning policies of banks especially in the industrial sector much earlier and their cheap monetary and financial policy has resulted in huge amount non-performing assets based on losses involved in full and final recovery of advances. An asset is called non-performing if interest or installments of the principal due remain unpaid for more than 90 days. In China the NPA level was significantly very high during 2001-2004 and the same was recorded for more than 25%.

On the operational side, in exceptional cases, the government of China had borne the financial losses of debt discounting. Even debt/equity swap were also allowed in case of potential growth opportunities. The Government pumped in $45 bn for recapitalisation of State owned banks: Bank of China, Agricultural Bank of China, China Construction Bank and Industrial Commercial Bank of China and they were indeed successful in reducing their NPA by 2009, mainly by securitizing their debts (NPA assets) into equity by transfer of the secured assets to some privately managed specialists vehicles, that have clear mandate and expertise in restructuring of the corporate.

Presently, raising NPA is the core concern for India, as of Dec'2016 stressed assets (including both non-performing and restructured) stood at Rs.9.64Lakh Crore, which is almost 7% of India's Gross Domestic Product.

A comparative graph of NPA for India and China for the period 2001-16 is shown in figure 1.

Figure 1: Comparative Chart for NPA



Source: IMF

The RBI already instructed Indian banks in June 2017 to initiate stringent action and provide additional provisioning minimum Rs.81,000 crore towards 12 big ticket NPA accounts identifying to National Company law Tribunal under the insolvency and bankruptcy code. Moreover India rating Ind-Ra in its report highlighted that Indian banks over all exposure in unorganized sector is Rs. 7.70 lac crore as of September 2016 and almost 35% of the same may slip into substandard towards over the next 12 to 18 months. In August 2017, RBI has further declared the list of 50 companies of top defaulters and directed banks to initiate insolvency proceedings under the provisions of insolvency and bankruptcy code, 2016 (IBC) after list of 12 defaulting companies as mentioned above. This stand may dissolve 60% of total Rs.7,00,000 crore of NPA of Indian banks, which were in their books for almost a decade.

Thus, We may expect some more stringent initiatives from Government of India to check the situation. Government has already under their Indradhanush plan declared to infuse fresh capital in banks to the tune of Rs.10000/-Crore per year. However, As per the Moody's report Indian Government need to infuse additional capital to the tune of Rs.95,000/-Crore in banks to stabilize them within next 2-years.

- **Currency flexibility** :

China adopted a regime of fixed exchange rates for its currency since 1978. Yuan (Renminibi) has been pegged at 8.28 to US$ holding a forex reserve of more than 470 billions. Due to this it remained gross under valued for many years. This gross under valuation of Yuan was main reason for China's huge FDI inflows and competitiveness of exports with US. In order to move its exchange rates more flexible to demand and supply the Yuan has been appreciated in terms of dollar on 27th July 2005.[15] Now it is set at 8.11 per US$ i.e. 2.1% appreciated in its value. This appreciation resulted in cheaper imports reducing the cost of manufacturing and made Chinese exports expensive in US. PBoC (People's Bank of China) has also linked Yuan's value to a basket of currencies of its major trading partners.

On 11 August 2015 RMB central parity fixing mechanism and the decision of China to weaken yuan's reference rate by 1.9%, spread like a fire in the financial markets all over the world. This move was interpreted as an indicator that in order to encourage export by weakening the currency instead of implementing market oriented currency reform. The currency further depreciated by 3% (11-14 August 2015). In January 2016, the PBOC set the midpoint rate at RMB 6.5646 per USD, this was the lowest rate since March 2011 this move acted as shock to the financial market. Due to this move there were large capital outflows and a decline in Forex.

In order to be more transparent and to help anchor currency expectations as well as to smooth the transition phase to a more flexible regime the Trade Weighted Foreign Exchange Index was formed on 11 December 2015 making it easy for PBOC to usher RMB lower against US dollar shifting its attention from CNY/USD to some basket measures. (China clears way for further Renminbi weakening 2015). The BOP data reflected a net FDI negative that is –USD 76 billion for the first three quarters in 2016. This was due to the weaker RMB paired with slow rate of return on investment due to over investment and over capacity, which led to repatriation of FDI profits.

According to Robert Mundell, it is impossible for a country to have complete control of the three monetary policy instruments a fixed exchange rate, an open capital account nad an independent monetary policy, his is called the "impossible trinity". China controlled all the three in its old model since 1978 through sterlisation that enabled it to retain monetary autonomyand the exchange rate control in the form of huge capital flows. Since 2001 acquisition in WTO China gradually liberalized its capital and financial account, RMB was included in IMFs Special Drawing Rights (SDR) basket in October 2016 the scenario of China changed.

India has already adopted floating exchange rate flexibility in 1992 under which control on exchange rate rates can be exercised through interest rates, CRR, and the bank rate. In such a flexible regime these monetary tools are very useful in ensuring control on currency values in short run.

Appreciation of Indian Rupees after mid 2007 till January 2008 was allowed to happen to reduce the burden of soaring crude oil price in international market and overflow of FIIs investments. US recession finally gripping the international economy is on the other side, had made Indian rupee to have another downturn during 2008. In 2011-2012 it depreciated by 30% to US$, the value of 1 USD is Rs.64.03, August 2017. Indian Forex reserve remain shallow to around $ 260 bn against in China $ 1,950,000 mn by December 2008. China Reserves rose $21 billion in April 2017 to $3.03 trillion, compared with an increase of $3.96 billion in March 2017 to $3.009 trillion. India's forex reserves, surged by $1.536 billion to touch a new record of $392.867 billion during the week to 28 July 2017, Reserve Bank of India (RBI).

RBI did not try to prevent the rise of rupee even though it was overvalued in real terms. The real effective exchange rate against a basket of 36 other currencies was 118.38 in February 2017—one of the highest levels. Indian exports had recovered in the past few months but the currency overvaluation has most often led to higher current account imbalances in medium term. The reason could be the excess liquidity that is currently spilling around in the Indian financial system.

The demonetisation in early November 2016 forced citizens to place their money holdings with banks. Restrictions on withdrawals meant that the composition of broad money changed radically as demand deposits substituted currency in portfolios. Banks remained cautious about lending the money deposited because it was not sure how long this money would remain with them.

RBI tried to wipe some of the excess liquidity with the banks through the issue of market stabilization bonds. But there is still too much liquidity when the monetary policy outlook moved from accommodative to neutral.

Aggressive buying of dollars by the RBI at this point will add to the excess liquidity. Informal estimates suggest, excess liquidity is to the tune of Rs.3 trillion.

Hence RBI did not intervene in foreign exchange because it doing so will further exacerbate the excess liquidity problem, because it will have to release rupees into the market whenever it buys dollars. Sterilization firepower is limited , which is the reason it had to issue market stabilization bonds in the.

To get the right balance the RBI should see loose money market conditions do not feed into inflation.

More of the current problems arise from the effects of the demonitisation, especially the excess liquidity which has been created. India is not yet facing the most extreme forms of the impossible trinity—the ability to run an independent monetary policy in a world of capital mobility as well as flexible currencies.

- **Round Tripping:**

Significant part of People's Republic of China (PRC)'s FDI inflows belongs to the return of the Chinese capital that has gone aboard escaping the foreign exchange control. Thus the capital originally created in PRC manages to flight abroad and stays aboard waiting for opportunities to return back to PRC.

In the past two decades, about 40% to 60% of PRC's FDI inflows were from Hong Kong, China (People's Republic of China (PRC)'s official report). Half of Hong Kong, China's FDI to PRC reported by PRC could not be verified from the related statistics collected in Hong Kong, China.

- Hong Kong was the PRC's largest source of realised FDI, accounting for about 51.7% of the national total as at end-2016.

- The investments concentrate largely in the Guangdong Province. The cumulative value of Hong Kong's realised direct investment in Guangdong was estimated at HK$1,984.5 billion (US$255.9 billion), accounting for 63.8% of Guangdong's total, at end-2016. About 140,000 Hong Kong-invested enterprises have been approved cumulatively by the Guangdong Province according to the statistics of the Guangdong Province, at end-2016.
- In the early years Investments in the Mainland were mainly industrial investment primarily outward processing arrangements. Over the years, it has extended the scope of investments in the Mainland to other sectors such as hotels, real estate, retail trade, financial services, communications etc.
- A Hong Kong company can pose as a "foreign" investor and enjoy benefits such as cheap land that a purely domestic investor may not get. Other Hong Kong affiliates may be intended to mitigate the perceptual drawback of an investor's origin from mainland China.

Clearly Hong Kong, China is crucial in understanding PRC's round tripping capital flows. It is not alone in facilitating capital creation, capital flight, and the return of flight capital through round tripping FDI. The offshore financial centres, such as British Virgin Islands, Bermuda, and Cayman Islands, have been playing more and more important role, particularly in facilitating legitimate round tripping capital flows for the purpose of listing the Mainland PRC companies in Hong Kong, China and other overseas stock markets.

According to PRC's official definition, FDI refers to the investment in three legal types of foreign invested enterprises (FIEs) in PRC:

1. solely foreign funded enterprises(FFE),
2. sino-foreign joint ventures and
3. sino-foreign cooperative ventures.

The foreign investors in FIEs include any foreign enterprise, economic entity or individual as well as the Hong Kong, China, Macao and Taipei, China compatriots and the Chinese enterprises registered outside PRC. FDI must be invested in the form of spot foreign exchange, in-kind, or technology investment. The re-investment of the profits by FIEs and the funds borrowed from overseas by the FIEs for their PRC projects can also be counted as FDI.

The difficulty of estimating the scale of PRC's round tripping lies in the fact that the definition and nature of round tripping are not clarified conceptually. The two types of round tripping are differentiated as under:

1. The first type of round-tripping, e.g. 'round tripping for escaping regulation', creates no value added but facilitates the private sector's effort to get around the legal or administrative constraints/weakness, such as barriers to trade, high taxes, lack of property rights protection, etc.
2. The second type of round tripping, e.g. 'round tripping for value added services', creates value added much like the financial sector's role for the real economy. Most cross-border mergers and acquisitions involve this type of round tripping of capital for value added financial services. Hong Kong, China as a modern international financial and trade centre is at the heart of the "round tripping for value added financial services." **The round tripping is not only profit making but is also related to safety of the capital and risk management.**

CONCLUSION –

Though the policy atmosphere in China for attracting FDI is more stringent relative to that in India, it still makes China the favorite of foreign investors, enabling it to gain FDI in unmatched volume year after year due to basic features that help attract FDI to China, besides a stable political structure, include lower commodity and utility prices, lower indirect taxes, lower import duties on raw materials, higher labour productivity and low capital investment requirements.

To encourage foreign investments in technology development and innovation, China has initiated a transformation from low to hi-tech industries with comparatively more lucrative tax incentives to lure foreign investors. Equipment (and related technology), components and spares brought into China by the foreign invested R&D centers are exempt from import duty. Besides, China still extensively uses fiscal and other fillips to encourage some specific types of investment for instance, export-oriented and technologically advanced FDI and to guide the flows into certain targeted regions and industries.

Hence, China attracts foreign investors not only by projecting its inherent strengths but also by creating a congenial economic atmosphere. The setting up of SEZs, where business is regulated by an independent authority, has been one of the major reasons for China's FDI successes.

Following the same, **India has started** several initiatives like preference to 'Buy (Indian)', 'Buy & Make (Indian)' & 'Make' categories of acquisition over 'Buy (Global)' category, thereby giving preference to Indian industry in procurement, this is a clear indication that Government is interested in Long term capital investment by FDI. On the contrary, the policy-makers impose obligations on foreign firms even for transfer of technology to reduce trade deficit. Furthermore, to manage and reduce lack of harmonization in government policies

Government has implemented Goods & Service Tax (GST) as the major initiative and we may expect a better ranking in next FDI Confidence Index out of the reforms.

It is pertinent to note that India has an edge over China vis-à-vis managerial skills, large English speaking population, and highly educated workforce low salaried workforce in the field of medicine, engineering and software.

Hence, India is also paving the way for more optimistic inflow of FDI on the back of persistent reforms & government initiatives towards developing a better business environment and transparent Policies.

APPENDIX

Exhibit A.1 : A Comparative of FDI Components

	IMF	**China**	**India**
Equity Capital	Equity capital of unincorporated entities	Equity capital of unincorporated entities	Equity capital of unincorporated entities
	Non-cash acquisition against technology transfer, plant and machinery, goodwill, business development and similar considerations	Non-cash acquisition against technology transfer, plant and machinery, goodwill, business development and similar considerations	--------
	Control premium	Control premium	Control premium
	Non-competition feesm	Non-competition feesm	Non-competition feesm
Reinvested earnings	Reinvested earnings of incorporated entities	Reinvested earnings of incorporated entities	Reinvested earnings of incorporated entities

	Reinvested earnings of unincorporated earnings	Reinvested earnings of unincorporated earnings	Reinvested earnings of unincorporated earnings
	Reinvested earnings of indirectly held investment enterprises	Reinvested earnings of indirectly held investment enterprises	--------
Other capital	Short-term and long-term inter-corporate borrowing	Short-term and long-term inter-corporate borrowing	Short-term and long-term inter-corporate borrowing
	Trade credit	Trade credit	---------
	Suppliers credit	Suppliers credit	Suppliers credit
	Financial leasing	Financial leasing	Financial leasing
	Financial derivatives	Financial derivatives	---------
	Debt securities	Debt securities	--------
	Land and buildings	Land and buildings	--------
Imported Equipment	----------------	Imported Equipment	--------
Round Tripping of Capital	-----------------	Round Tripping of Capital	--------

Source: Redefining FDI: Can the Elephant Trump the Dragon? India Brand Equity Foundation (IBEF), CII, pg 9, www.ibef.org/artdisplay.aspx?cat_id=410&art_id=5634, accessed on 10 February 2008, & Bajpai Nirupam and Dasgupta Nandita,

Table – 1 :: Different Forms of Foreign Invested Enterprises (FIEs)

 # Liberalized Capital Requirement for WFOE

It is very important to choose an appropriate amount towards investment as registered capital. If the amount is too little, then the WFOE application may be rejected by officials and they may also put the company at risk of

insolvency. However, if the amount is too much, then the company risks having idle funds and missing opportunities.

More flexibility offered recently by implementation of PRC Company Law to investors, which is as follows:-

- As of March 2014, there is no minimum registered capital requirement, except for a few select industries;
- Investors can choose the period of contribution of the capital, which must be laid out in a schedule of contributions specified in the Articles of Association; and
- It is no longer required that 30 percent of registered capital consist of a cash contribution.

Business scope

The business scope represents a company's activities within China, which directly affects the legal operations of a company and the affirm company's ability to issue official invoices (fapiao) to clients. Once written and approved, the same is printed on the company business license. Therefore, business scopes should be prepared and agreed on in advance of incorporation. It is connected to the Catalogue, which lists the encouraged, permitted, and prohibited industries for foreign investment into China.

Additional Tax Benefits-

- WFOE in China, investors have to inevitably incur costs for pre-operation period (period start from the establishment date on the business license, or the day that the company gets its name confirmation from the AIC. The end date is when the company issues its first invoice, or first generates revenue) and may get benefit in income tax on some of the costs incurred in pre-operation period – such as wages, training fees, printing fees, transport fees, registration fees, and purchases of items not considered fixed assets.
- During its pre-operation period, WFOE is not insisted for registration as general Tax Payer, However, under China's reformed VAT system, it is required for getting the tax benefit as mentioned in the above point.

TableA.1 : Foreign Direct Investment Indicators in India and China

Item	2008	2009	2010	2011	2013	2014	2015	2016
FDI US mn $	108312	95000	114734	123985	123911	1235 8500	135610	133700
FDI stock	378083	473083	578818	711808	956793	1085293	1220903	1354404
Number of Green Field Investments	1624	1195	1344	1409	1256	1080	876	800
Value of Cross Border M&A Sales(In Mn $)	236	142	155	151	31066	56775	12439	5887
Value of Cross Border M&A Purchases (In Mn $)	69	97	150	143	51526	39250	51117	92221
India								
FDI US mn $	43408	35596	24159	31554	28199	34582	44064	44686
FDI stock	123288	163959	197939	201725	226549	253120	282609	318502
Number of Green Field Investments	1023	761	774	932	589	713	723	847

Value of Cross Border M&A Sales(In Mn $)	136	104	115	131	4644	7857	1323	7841
Value of Cross Border M&A Purchases (In Mn $)	163	56	141	99	1922	1021	-612	8581

Note: YOY – Year on Year Growth

* Figure has been taken from Chary, S.Narshimha & Gangadhar, V. DFI in developing Asia: An analytical study of India and China, , pg.94, from Management and Accounting Research.

Source: WIR 2010-2017

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