

## India growth story has a 'beneficial ownership' hurdle

(The Hindu, 15/06/24)

Foreign investments will play a crucial role in aiding the government's goal of a \$5 trillion economy by the end of the financial year 2025-26.

The Indian Foreign Exchange Management (Non-debt Instruments) Rules, 2019 ("**FEMA NDI**") has posed a significant challenge for Indian companies, especially start-ups and smaller enterprises seeking foreign investments.

### What is the importance of foreign investment in India's growth story?

- **Money for development:** Foreign investment brings in additional funds that can be used to finance new businesses, improve infrastructure, and create jobs. This is especially important for a developing country like India.
- **Expertise and technology:** Foreign companies often bring advanced technology and expertise to India. This can help Indian companies become more efficient and competitive in the global market.
- **Increased competition:** Foreign investment can lead to more competition in the Indian market. This can drive innovation and lower prices for consumers.
- **Boost in exports:** Foreign companies may set up manufacturing units in India to take advantage of the large domestic market and lower labor costs. This can lead to an increase in India's exports and helps India integrate into global value chains.
- **Skill development:** Collaboration with foreign firms exposes the Indian workforce to global standards, leading to skill upgradation and improved human capital.
- **Improving business environment:** To attract foreign investment, India has undertaken various reforms to improve the ease of doing business. These reforms benefit both foreign and domestic investors.

### What are the concerns associated with foreign investment ?

- **Dependence on foreign capital:** Excessive reliance on foreign investment can make a country vulnerable to external shocks and capital flight during global economic uncertainties.
- **Economic sovereignty:** Large-scale foreign investment in strategic sectors can raise concerns about the influence of foreign entities on domestic economic policies and decision-making.
- **Political Influence:** Foreign investors, particularly large multinational corporations, can wield significant political influence, potentially swaying policy decisions in their favor, which may not always align with national interests.
- **Exploitation of resources:** There's a fear that foreign companies might exploit India's natural resources without giving back sufficiently i.e Foreign companies may repatriate a significant portion of their profits back to their home countries, limiting the benefits to the host economy.

- **Unequal benefits:** Large corporations might benefit more from foreign investment than small and medium businesses.
- **Environmental and social impact:** Some foreign investments, particularly in extractive industries or large infrastructure projects, can have adverse environmental and social consequences if not properly regulated.
- **Loss of Cultural Identity:** The influx of foreign companies and their products can lead to cultural homogenization, where local customs, traditions, and businesses may be overshadowed by global brands and practices.

### What is the issue with the 2019 FEMA NDI Rule?

FEMA NDI 2019 Rules, amongst others, says that any investment in an Indian company needs government permission if the money comes from neighboring countries or if the person really controlling the money (the "beneficial owner") is from a neighboring country.

- This was promulgated during the COVID-19 pandemic to curb opportunistic takeovers or acquisitions of Indian companies during difficult times.

However, this has created significant challenges for Indian companies, especially startups, seeking foreign investment. The key problems are:

- The term "**beneficial owner**" is not defined, leading to uncertainty about who needs government approval.
- The prior government **approval process is time-consuming** and has a high rejection rate. For ex: Proposals worth ₹50,000 crore from the Neighbouring Countries are either pending, withdrawn or rejected; and a staggering 201 applications have been rejected in the past three years.
- The **fin**es (of up to three times the investment received) for non-compliance can be crippling for startups.

The proposed solution includes:

- Defining "beneficial owner" with clear ownership thresholds and control tests.
- Establishing a consultation mechanism with regulatory authorities to clarify ambiguous cases.

*Can you answer the following question?*

*Should the Indian government prioritize attracting foreign investment at all costs, or should it focus on fostering domestic investment first?*

China has adopted sophisticated grey-zone warfare tactics against Taiwan following the inauguration of new Taiwanese President Lai Ching-te, who has made pro-independence and secessionist statements.

### **What is Grey-Zone Warfare?**

- Grey zone warfare refers to a set of tactics and strategies that fall between traditional warfare and peacetime diplomacy.
- These actions are typically coercive and aggressive but are deliberately kept below the threshold of outright military conflict.
- The goal is to achieve strategic objectives without provoking a full-scale war or triggering a robust military response.
- In today's nuclear age, the price of traditional wars has become too high, and the danger of things getting worse is very serious. Because of this, countries are trying to achieve their goals by being aggressive in secret or by hiding.

### **What are the characteristics of Grey Zone Warfare?**

- **Ambiguity and Deniability:** Grey zone actors often try to obscure who is behind the attacks or actions. This makes it hard to attribute blame and discourages a strong response
- **Incrementalism:** These tactics are usually implemented incrementally, with gradual escalations that are carefully calibrated to avoid crossing the threshold that would trigger a significant military response
- **Exploitation of Legal and Political Gaps:** Grey zone activities often exploit gaps in international law and political frameworks. The actions are designed to operate within or just outside existing legal boundaries, complicating legal responses.
- **Proxy forces:** Grey zone tactics may involve the use of proxy forces, such as militias, paramilitary groups, or non-state actors, to carry out actions on behalf of the aggressor state.
- Here are some examples of grey zone tactics:
  - **Cyberattacks:** Disrupting critical infrastructure or stealing sensitive data.
  - **Proxy wars:** Supporting rebel groups or militias to fight a rival nation indirectly.

- **Economic coercion:** Using trade restrictions or financial pressure to influence a nation's policies.
- **Disinformation campaigns:** Spreading false information to sow discord and undermine public trust.
- **Political Subversion:** Efforts to destabilize or influence political systems through support for opposition groups, interference in elections, or fostering corruption.

· **Real Life Examples:**

- Russia's annexation of Crimea in 2014, involved the use of unmarked troops (often referred to as "little green men"), cyber operations, and disinformation campaigns to achieve territorial and political objective without full war.
- China- Taiwan: Chinese Army conducts training drills to demonstrate combat readiness, while 3D animations and videos depict potential missile strikes.
- China in South China Sea: Building artificial islands and militarizing them, using its coast guard and fishing fleets to assert territorial claims, and conducting cyber espionage and economic coercion against neighboring countries.

**Why dealing with Grey Zone Warfare is a challenging one?**

- **Blurred Lines & Attribution:** Cyberattacks, disinformation campaigns, and economic pressure can be disguised or made to appear like unrelated events. This makes it difficult to pinpoint the culprit and justify a strong response.
- **Escalation Uncertainty:** Responding forcefully to a grey zone tactic risks escalating the situation into a full-blown conflict. This is a gamble the targeted nation has to weigh carefully. Conversely, not responding can embolden the aggressor and leave you vulnerable.
- **Complex Coordination:** Grey zone conflict tends to escalate in multiple dimensions. Effective response to grey zone tactics requires coordinated efforts across multiple domains, including military, intelligence, cyber security, economic policy, and public diplomacy. Achieving this level of coordination within and among nations is complex.
- **Domestic Pressure:** Disinformation campaigns can sow discord within a nation, making it difficult to build a unified response. Citizens might disagree on the severity of the threat or the best course of action.

- **International Cooperation:** Countering grey zone tactics often requires international cooperation to expose the aggressor and hold them accountable. However, securing coordinated action can be challenging due to varying national interests and political agendas.

#### **How to deal with Grey Zone Warfare?**

- **Improve situational awareness** by investing in intelligence, surveillance, and reconnaissance capabilities to detect and attribute grey zone activities.
- **Non-Kinetic Measures:** Targeted sanctions, diplomatic rebukes, and exposing disinformation campaigns can be effective tools to counter grey zone tactics without resorting to military force.
- **Economic Diversification:** Reducing dependence on a single trade partner or economic sector lessens vulnerability to economic coercion.
- **Media Literacy:** Educating citizens on how to identify and counter disinformation campaigns is essential. This involves promoting critical thinking skills and using reliable news sources.
- **International Collaboration:** Engage in multilateral efforts, through alliances and partnerships, to establish norms and rules for acceptable behavior in the grey zone

*Can you answer the following question?*

*Does Grey Zone Warfare represent a new, dominant form of future conflicts, or is it a temporary phase in warfare's evolution?*