India’s dramatic spike in foreign direct investment (FDI) starting in August 2020 was a welcome counternarrative to the declining gross domestic product (GDP). The Modi government’s early push to liberalize foreign investment restrictions, the prime minister’s personal courtship of major investors, and key domestic reforms were important precursors. However, India has seen a precipitous decline in FDI inflows in recent months. Renewing investor interest requires a mix of federal-level policy reforms and state-level operational improvements. Haste is required as multinational companies increasingly look to markets outside China for growth.

After coming to office in May 2014, the Modi government moved with unprecedented speed to remove impediments to FDI. In its first three years in office, India made 37 sectoral relaxations in FDI rules, far outpacing the number of sectoral relaxations in the entire six-year run of the Prime Minister Vajpayee government (29 changes), and equal to the sectoral relaxations in the full 10-year run of the Prime Minister Singh government.

However, starting with the Modi government’s fourth year in office, there were few steps to further liberalize FDI regulations. Key domestic reforms like the goods and services tax (GST) and the insolvency and bankruptcy code (IBC) helped boost the Modi government’s reform credentials. Many factors critical to business success are governed by India’s state governments. Steps by the Modi government such as ranking Indian states’ business environments under the Business Reforms Action Plan (BRAP), while imperfect, fomented transparency and some level of competition among states to improve.

India’s FDI inflows saw a quick jump, crossing the $40 billion mark in 2016, then spiking 31 percent to over $62 billion in 2020. The nation’s 12-month inflow hit a record of $72.4 billion in June 2021. The United Nations Conference on Trade and Development (UNCTAD) noted in its World Investment Report 2021 that a great deal of this FDI influx, overall, was from share acquisitions instead of greenfield investment. But this does not account for the entirety of India’s success in bringing in FDI.

**KEY DATA**

- **+45.3%**
  - U.S.-INDIA GOODS TRADE, 12-MONTH COMPARISON, PER U.S. CENSUS BUREAU
- **-19.4%**
  - FOREIGN DIRECT INVESTMENT, 12-MONTH COMPARISON, PER RBI
- **$1.4 bn**
  - FII ASSETS NET FLOWS, LAST 12 MONTHS, PER NSDL
However, since last June, the average monthly FDI has declined. Just six months later, the 12-month FDI inflow had dropped by one-quarter, down to $52 billion. While this is still a fine total by India’s historical standards, it indicates that action is required to quickly rebuild interest and confidence among investors. This dip comes at a time when a larger share of multinational corporations are shifting new investments away from China—the market that had been a powerful magnet for global investments in emerging markets in recent decades.

The union budget and accompanying prospective reforms in Finance Minister Nirmala Sitharaman’s February 1 budget speech lacked any specific provisions related to foreign investors. But the process to win back a larger share of foreign investment is not impossible. It will take a concerted effort across multiple workstreams. The Modi government should consider the following recommendations:

1. **“Do no harm”:** The government should move cautiously on pending policy issues where investors warn of a chilling effect. Notably, this includes some of the damaging cross-border data provisions of the pending Personal Data Protection Bill. A real cost-benefit analysis, beyond the parliamentary review, is required. A misstep is too dangerous.

2. **Move quickly on remaining FDI barriers:** Even after 30 years of progressive liberalization, India still has dozens of sectors with FDI caps or other forms of tilting regulations away from foreign investors.

3. **Avoid poison pills and half-measures:** Recent liberalization measures in sectors like insurance and geospatial data include provisions that damage foreign firms’ ability to operate in the market. Such reforms must avoid unnecessary poison pills. A year after the government increased the FDI cap in insurance, few foreign firms have bothered to step up their investments because of damaging policies adopted just afterward that target foreign-invested firms.

4. **Improve FDI data and transparency:** The government still provides little transparency on where FDI is coming from, which states are attracting FDI, and which sectors. The Department of Industry and Internal Trade (DPIIT)’s quarterly FDI statistics still list Singapore and Mauritius as among the top investors due to provisions in their tax treaties. The sectoral breakdown lumps together an incredibly diverse set of services including banking, insurance, and outsourcing. And the chart showing which states are attracting FDI only counts where filings are made, not where a physical investment is made.

5. **Push states to improve:** The DPIIT’s nascent work to catalog state business policies under the Business Reform Action Plan (BRAP) needs new energy. The rankings have only been released three times in seven years and have not been assessed since 2019. While the model was imperfect—largely due to self-declaration by states—it was a good start.

6. **Improve trade integration:** While necessary for India’s trade deficit with the world, trade barriers are a real deterrent to India’s integration in global supply chains and discourage related foreign investment.

Without credible action, India may continue to stumble along as a modestly important destination for foreign investment. However, current shifts in global supply chains are a generational opportunity to grab large shares of investment in short order. Let’s hope the spike in FDI over the last 18 months was simply a taste of what is to come.