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Why MNCs are quitting India

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Eight years after Prime Minister Narendra Modi first urged multinational companies to "Make in India", Asia's third-largest economy is witnessing many foreign firms give up on the country.

A slew of big names including German retailer Metro AG, Swiss building-materials firm Holcim, US automaker Ford, UK banking major Royal Bank of Scotland, US bikemaker Harley-Davidson and US banking behemoth Citibank have chosen to pull the plug on their operations in India or downsize their presence in recent years.

This is a worrying trend at a time when India is trying to position itself as an alternative to China, in a post-Covid world where many MNCs are looking to diversify their supply chain.

A total of 2,783 foreign companies with registered offices or subsidiaries in India closed their operations in the country between 2014 and November 2021, Commerce and Industry Minister Piyush Goyal told Parliament late last year. That is not a small figure, given that there are only 12,458 active foreign subsidiaries operating in the country. While the reasons are company-specific in some cases like restructuring to curb losses, failure to crack the price-sensitive Indian market or a pivot towards green businesses, several have also given up on India due to regulatory flip-flops, high tariff barriers, red tape, perplexing land policies, infrastructure issues and others tied to the ease of doing business. Minister Goyal's office did not respond to a request seeking comment.

A view of the Ford manufacturing unit in India. BLOOMBERG FILE PHOTO

INSIGHT

While the ease of doing business has definitely improved in India, constant regulatory changes have given rise to uncertainties. "The regulatory changes have taken some time to get used to. From incorporation to assessment, the government aims to automate processes. However, we have seen that the implementation of these processes is not up to the mark," Neeraj Agarwala, Partner, Nangia Andersen LLP, tells *DH*.

To make things worse, there are 26,134 imprisonment clauses in India's business laws, according to an Observer Research Foundation report that highlights the risks faced by entrepreneurs and corporations in doing business in India.

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Regulatory hurdles, tariff trauma

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"India suffers from 'regulatory cholesterol' that is getting in the way of doing business. The legislations, rules and regulations enacted by the union and state governments have over time created barriers to the smooth flow of ideas, organisation, money, entrepreneurship," says Gautam Chikermane, Vice President at the Observer Research Foundation, and Rishi Agrawal, co-founder and CEO at Avantis RegTech.

PM Modi's dream of making India an electronics manufacturing hub could face serious obstacles if the country does not work on fixing these issues.

This might also explain why some of the world's biggest chipmakers have not warmed up to India despite its government rolling out a red carpet for them by approving a $10 billion incentive plan last year.

"All the top guns in the semiconductor majors are Indian, why was there a need for them to leave the country 30 years back, that was because there was a lack of infrastructure, right? So if these biggies see a potential in the next 20 years, only then will they invest," says Arokiaraj Jesudoss, Senior General Manager, Research & Development, 3M.

Apart from incentives, there is a need to establish the country as a thriving market. "Only those companies that have well-established technology or don't want to develop much but want to transfer second-grade technology to India will invest. So, once we get that and fulfil the domestic demand, investments will flow in, as and when the giants of the game see potential business in India," he says.

Policy flip-flops

Companies across the globe find India hard to ignore due to its vast population and huge market potential, but doing business here has not been easy for many.

"India is probably the highest tariff nation in the world," former US President Donald Trump said in New Delhi two years ago, while lamenting the high import tariff that Harley-Davidson had to pay in India.

Regulatory flip-flops have also driven companies out of India.

"India's struggle has been its inability to simplify regulations. Complex framework causes confusion and proves to be tedious for investors. However, simplification leads to exploitation and tax leakage. India needs to find a healthy balance," Agarwala says.

In February this year, the government paid British firm Cairn Energy Plc Rs 7,900 crore to refund taxes it had collected to enforce a retrospective tax demand. Last year, it passed legislation to drop outstanding claims against MNCs including telecom giant Vodafone, pharma major Sanofi and brewer SABMiller.

"Retrospective taxation (such as in Vodafone's case) prohibits entry," Indian School of Business Professor Shekhar Tomar tells *DH*.

India could certainly do more to attract more MNCs.

"It is not a one-day process. Decrease regulation, don't change rules too often, avoid retrospective taxation. For instance, stability in tariff structure is very important to allow MNCs to integrate India in global value chains. Similarly, many laws vary by state and they need to play a proactive role to attract MNCs," Professor Tomar says.

Clearly, India has a long way to go on that front.

Last month, Tesla said it had put its plans to sell electric vehicles in India on hold, after failing to convince the government to cut the prohibitive import taxes. The US automaker wanted to test the waters in India by selling its EVs made abroad and sought a lower tariff. But the government wanted it to make its vehicles in India first before granting it what it wanted.

India levies 100% tax on imported cars with a price tag over Rs 30 lakh, while cars cheaper than that are taxed at 60%.

"Cutting duties on EVs even to 25% from the current levels which are as high as 100% wouldn't pose a threat to domestic players, but would help to drive investment and speed up the creation of the ecosystem," Gurpratap Boparai, the MD of Skoda Auto Volkswagen India told Bloomberg last year, when it backed Tesla's push for a tax cut on EV imports.

Not all agree. "I don't believe there is a need to give special incentives to any one single company," says Manoj Garg, Investment Director, WhiteOak Capital Management. "Some of the large global companies have entered China not because the local government has given them special incentives or privileges but because they saw potential for demand."

When asked if he would consider setting up a factory in India, Tesla CEO Elon Musk tweeted last month that the automaker would not set up a manufacturing plant, "in any location where we are not allowed first to sell and service cars."

Musk will instead look for potential opportunities in Indonesia, known for its business-friendly policy and production of nickel, a critical ingredient in making EV batteries.

Musk is not the only one looking beyond India.

A Parliamentary Standing Committee report of 2021 titled "Attracting investment in post-Covid Economy: Challenges and Opportunities for India" pointed out that foreign companies that shifted their manufacturing bases out of China during the pandemic picked countries such as Vietnam, Taiwan and Thailand, and only a few came to India.

There are key challenges in attracting investment, including administrative and regulatory hurdles, inadequate and costly credit, tedious land acquisition procedures and inadequate infrastructural facilities, high logistics costs and a large unorganised manufacturing sector, the report said.

"The policy changes and the incentive schemes brought in by the government to overcome these challenges are welcome measures and are in the right direction. However, success depends on the implementation of the reforms," the committee pointed out.

Missteps

To be sure, many MNCs, especially carmakers, had to leave India because of their own inability to crack the world's fourth-largest auto market, resulting in poor sales.

"We have to remember that the Indian market, in general, is very price sensitive. Price, product and positioning are very important for sustainable growth in the Indian market," says Agarwala.

"There is definitely a lack of planning or understanding of the Indian markets among MNCs that have failed. The competition is also very high and most foreign companies struggle to meet customer expectations. Cultivating brand loyalty in the Indian market is also very difficult, especially when companies succumb to product modifications that is, making cheaper substitutes," he adds.

Many in the industry agree that the automaker exits were more due to failure to adapt to the market than any regulatory issue, highlighting the diverging fortunes of foreign automakers such as Ford and Hyundai in India.

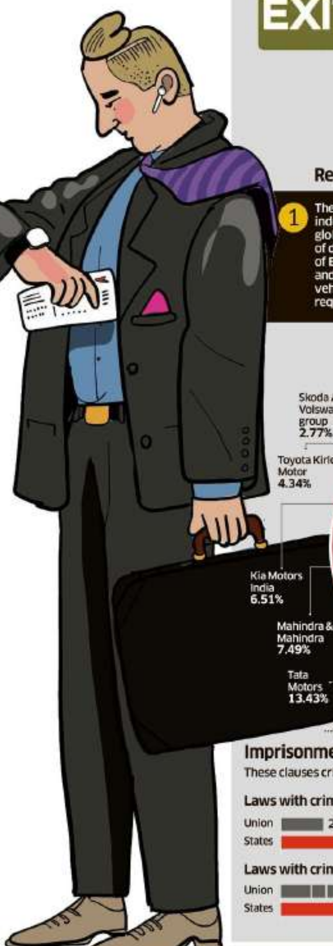
"You look at Hyundai, which is also an international company, but they managed to do well because of the range of products and developing ecosystem around the products," Garg says.

Some MNCs also left India because of a change in their own priorities.

For instance, Holcim decided to sell its Indian operations to billionaire Gautam Adani to move away from traditional cement and cater better to the growing demand for energy-efficient buildings, while Citibank left India as it decided to exit retail banking globally, according to Srinath Sridharan, a visiting fellow at ORF.

While he is not an advocate for preferential treatment of MNCs, he says two areas the country could work on to attract more international companies were simplifying regulations further and offering them single-window clearance.

"Do we have it currently? No. Would it be of help? Yes, it would be very pro-business. But at the same time, a smart businessman doesn't wait for that, he goes to a law firm," says Sridharan.



10,756 foreign companies were registered in India between 2014 and 2021

2,783 registered foreign companies have closed their operations in India in the same period

12,458 active subsidiaries of foreign companies operate in India

64,000 jobs were lost after automobile companies started quitting India after 2017

2,485 crores of investments were lost by car dealerships after 2017

India is the 4th largest automobile market worldwide

EXIT

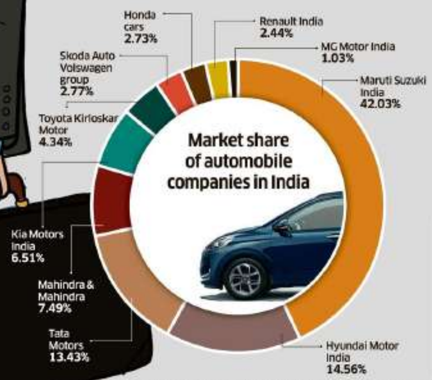
Automobile companies have been closing down since 2017

● Number of vehicle dealerships ● Employment loss ● Dealer investment (in crore) ● Customers affected (2012-2021)

	Ford India	General Motors	Harley-Davidson	Man Trucks	UM & Lohia	Total
Number of vehicle dealerships	170	142	34	38	80	464
Employment loss	40,000	15,000	2,000	4,500	2,500	64,000
Dealer investment (in crore)	2,000	65	70	200	150	2,485
Customers affected (2012-2021)	7,21,045	3,15,060	27,148	8,733	7,798	11,29,784

Reasons why auto companies are exiting the country

1. The automobile industry across the globe is seeing a lot of disruption in terms of EVs, connected and autonomous vehicles. This requires investment.
2. This is pushing companies to take a relook at their portfolio and long-term scope for market penetration.
3. Some companies are cutting costs by shutting down operations in certain countries.
4. Some companies have failed to understand the structure of the Indian market and the demand for smaller cars.
5. A few companies like Ford tried with small car ranges but options were limited to few products. Customers prefer cars within the three to seven lakh range in India.
6. There is a lack of an ecosystem with regard to servicing and support.



India has jumped 79 ranks in the ease of doing business since 2014

2014	142
2015	131
2016	130
2017	100
2018	77
2019	63

The web of business laws and compliances

Recommendations to ease regulatory framework

Single window clearance: A one-stop solution for investors and businesses to usher freedom from the legacy of running to govt offices for approvals and registrations.

Stable laws: The government is constantly making regulatory changes which have taken some time to get used to.

Imprisonment clauses are included in half of India's business laws

These clauses criminalise process violation and some punish minor lapses rather than wilful actions to defraud or evade. They impair the ease of doing business.

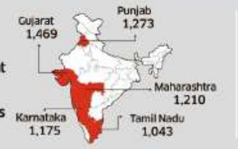
Laws with criminal clauses

Union	244
States	599

Laws with criminal compliances

Union	5,239
States	20,895

Five states have more than 1,000 imprisonment clauses in their business laws



Average number of jailing clauses per law

Labour	50.6
Industry specific	20.4
Finance and taxation	19.4
Environment & safety	15.1
General	12.8
Commercial	12.7
Secretarial	12.4

COMPILED BY VARSHA GOWDA

SOURCE: FEDERATION OF AUTOMOBILE DEALERS ASSOCIATIONS, JAILED FOR DOING BUSINESS BY ORF, WORLD BANK ANNUAL RATINGS

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