Working Paper 282

Facilitating Bilateral Investments between India and Germany: The Role of Negotiations and Reforms

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July 2014

INDIAN COUNCIL FOR RESEARCH ON INTERNATIONAL ECONOMIC RELATIONS

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Abbreviations

BIPAs	Bilateral Investment Promotion Agreements
BITs	Bilateral Investment Treaties
BTIA	Broad-based Trade and Investment Agreement
CECA	Comprehensive economic co-operation agreement
CEPA	Comprehensive economic partnership agreement
DIPP	Department of Industrial Policy and Promotion
DTAA	Double Taxation Avoidance Agreement
EU	European Union
FDI	Foreign direct investment
FICCI	Federation of Indian Chamber of Commerce and Industry
FIPB	Foreign Investment Promotion Board
FTAs	Free trade agreements
GATT	General Agreement on Tariffs and Trade
GATS	General Agreement on Trade in Services
GDP	Gross domestic product
GST	Goods and services tax
IGC	Intergovernmental consultations
IPR	Intellectual property rights
IT	Information technology
ITeS	Information technology enabled services
MAT	Minimum alternative tax
MFN	Most favoured nation
MoU	Memorandum of understanding
NCR	National capital region
NMIZs	National Manufacturing Investment Zones
NT	National treatment
OECD	Organisation for Economic Co-operation and Development
OFDI	Outward foreign direct investment

PTAs	Preferential trade agreements
RBI	Reserve Bank of India
R&D	Research and development
RTAs	Regional trade agreements
S&T	Science and technology
SEZ	Special economic zone
SMEs	Small and medium enterprises
T&M	Time and material
UK	United Kingdom
UNCTAD	United Nations Conference on Trade and Development
US	United States
WTO	World Trade Organization

Abstract

Germany is a large source country for investment and technology transfer into India and Indian investments in Germany are also growing overtime. The two countries have investment complementarities and, therefore, there is scope to enhance bilateral investments flows. However, there are many market access and operational restrictions, which impact the flow of bilateral investments. In this context, this paper aims to highlight the barriers to investment flows between India and Germany and suggest measures to address these barriers through bilateral trade negotiations and domestic reforms.

The paper found that policy uncertainty, rigid regulations and differences in technical and product standards are key barriers to bilateral investment flows between India and Germany. In addition, there are cultural and language barriers and lack of knowledge about the present policies and incentives in the two countries. Investment flows can be facilitated through inter-government agreements as they offer operational certainty and comprehensive trade agreements, which ensure a more liberal and predictable investment regime for the trading partners. The paper suggests that while some of the barriers can be addressed through domestic reforms and trade negotiations, there is also a need to enhance inter-government cooperation, government industry interactions and promote knowledge sharing between the two countries to facilitate investment flows.

JEL Classification: *F15, F21, F51, F53.*

Keywords: *Investments, India, Germany, International Agreements, Negotiations, Domestic Reforms*

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Facilitating Bilateral Investments between India and Germany: The Role of Negotiations and Reforms

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1. Introduction[2]

There is a significant amount of literature on the motives behind foreign direct investment (FDI) inflows. FDI can be market seeking – focusing on countries with large market size and prospective market growth (Behrman, 1972); resource seeking – providing access to natural resources, manpower, technology and organisational resources (Panayides, 2002); efficiency seeking – focusing on creating new sources of competitiveness for firms through specialisation, low cost of production and strengthening existing ones (Nunnenkamp, 2002) and strategic asset seeking – involving purchase of existing firms and/or its assets such as intellectual property, business knowledge or technology in the host country to make it more globally competitive (Behrman, 1972).

Factors that attract FDI are macroeconomic stability, economic reforms and autonomous liberalisation (Campos and Kinoshita, 2003), trade liberalisation (Mitra, 2012), good governance (Garibaldi *et al.*, 2002), low levels of country risk and high degree of freedom, well-developed infrastructure, public services and tax policies (Chang and Cheng, 1992) and an effective legal system (Perry 2000). Factors attracting potential investors to developing countries are changes in the policy environment (Amirahmadi and Wu, 1994; Banga, 2003; Chakraborty and Basu, 2002), liberalisation of FDI regulations (Nunnenkamp 2002), privatisation and globalisation of production (Chakraborty and Basu, 2002), output growth (Chakraborty and Nunnenkamp, 2008), establishment of global supply chains (Reardon *et al.*, 2004), simplified entry barriers and easing of laws and the tax system for foreign investors (Devajit, 2012). For developed countries, a freer business environment leads to outbound investments (Banga, 2003). Thus, the overall ease of doing business, i.e., an investor-friendly climate in the host country is likely to attract foreign investment.

Over the years, both developed and developing countries have liberalised their FDI regimes and pursued investment-friendly policies with the view to attract foreign investments. Regional, multilateral and bilateral agreements covering investments are seen as useful tools to promote a liberal investment regime and provide greater operational certainty to investment partners. Almost all major member countries of the World Trade Organization (WTO) have notified participation in at least one regional trade agreement (RTA) and some

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[2] The authors would like to thank Dr. Arpita Mukherjee, Professor, ICRIER and Dr. Jaimini Bhagwati, RBI Chair Professor, ICRIER for reviewing this paper and giving their valuable inputs and suggestions. This paper is based on findings of the study titled "Facilitating Investments between India and the European Union: The Case of Bilateral Investments between India and Germany", funded by Konrad-Adenauer-Stiftung (KAS). The authors are grateful to KAS for funding the study.

members are signatories of over 20 trade pacts.[3] Several nations have entered in Bilateral Investment Treaties (BITs) or Bilateral Investment Promotion Agreements (BIPAs) to provide investment protection and promote investments between countries.

India and the European Union (EU) (a regional bloc of 28 member states[4]) – are actively engaged in bilateral and regional agreements. India and the EU are negotiating a Broad-based Trade and Investment Agreement (BTIA) to broaden bilateral commercial and economic relations. The BTIA negotiations began in 2007 at the seventh India–EU summit held at Delhi. The BTIA is a comprehensive WTO+ (plus) agreement that will cover trade in goods, services, investment, trade facilitation measures, government procurement, labour standards and sustainable development, among others. If successfully negotiated, this will be the EU's first trade agreement with a large and growing emerging market. This will also be India's first trade agreement with a large trading block, which is also one of its largest trading and investment partners. This legally binding agreement would cover almost a fifth of the world population and, therefore, its impact and implications (both positive and negative) would be significant (Singh, 2009). Even though the negotiations have not progressed much over the last year, it is likely that the new Government and their policy reforms would renew the interest of the EU businesses in the Indian market, giving an edge to the negotiations again.

Among the EU Member States, Germany is India's largest trading partner and a major foreign investor. The bilateral merchandise trade and investments between India and Germany has increased overtime. Germany is also leading source of technology transfers in India. Germany is an export-oriented country with strong manufacturing competence, but the country is facing labour shortages, escalating labour costs and a saturated domestic market. Unlike Germany, India is a large and unsaturated market that is an attractive destination for FDI (Ernst & Young, 2012). After the liberalisation in the 1990s, the new policy regime in India placed an emphasis on attracting foreign investment (Rao and Dhar, 2011). In addition, a few large Indian firms are investing abroad in countries such as Germany for acquiring latest technology and build physical infrastructure and research and innovation capability (Tiwari, 2012). Given this, there is scope and potential for bilateral investments flows between India and Germany.

In the past, a major part of the German investment was in neighbouring countries within EU Member States, but now East Asian, South Asian and Southeast Asian markets are expected to become important destinations for German outward foreign direct investment (OFDI)[5], since they are growing and unsaturated economies. Moreover, countries such as India and China have large domestic markets. German FDI is primarily market seeking (Deutsche Bundesbank, 2006) and India offers a large consumer market (Ernst & Young, 2013). India needs investment in infrastructure not only to meet the demands of its growing population,

[3] WTO, *http://www.wto.org/english/tratop_e/region_e/regfac_e.htm* (last accessed on June 12, 2014).

[4] The EU Member States include Austria, Belgium, Bulgaria, Croatia, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Poland, Portugal, Romania, Slovakia, Slovenia, Spain, Sweden and United Kingdom.

[5] Indo-German Chamber of Commerce (2010).

but also to support its manufacturing and services sectors (Ernst & Young, 2013). Investments from Germany are likely to benefit India in this regard. Investments and joint ventures in India provide good business opportunities for German medium-sized companies (Deutsche Bundesbank, 2006) to expand their global presence.

Since Germany is a key trade and investment partner for India within the EU, the India-EU BTIA is likely to bring far-reaching impact on bilateral investments between India and Germany. In the past, several measures have been taken by the two countries to facilitate investment flows. In 1998, Germany signed a Bilateral Investment Promotion Agreement (BIPA) with India that aims to facilitate promotion and protection of investments in the two countries. India also has a Double Taxation Avoidance Agreement (DTAA) with Germany (1998).

Given this background, the objective of this paper is to compare the Indian and the German markets, analyse the present trends in the investment flows between India and Germany, examine their negotiating positions with respect to investments in different bilateral agreements, understand the barriers and potential for investment between India and Germany and suggest reforms and negotiating strategy to address these barriers and exploit the potential. The paper is based on secondary data and information and a primary survey conducted in India and Germany.

2. Overview of Indian and German Market

Germany and India are at two different stages of development. While one is a developed country and the other is an emerging market economy. In terms of nominal gross domestic product (GDP), the German economy in 2005 was about three times the size of the Indian economy. Even though Germany has been hit hard by the eurozone crisis, its GDP was about twice the size of India's in 2013. In terms of nominal GDP per capita as well, Germany is about 30 times the size of India.

Trade is an important component of the GDP of India and Germany. The share of trade to GDP was 98 per cent in case of Germany and to 55.4 per cent for India in 2012.[6] While Germany has a positive trade balance in its global merchandise trade, India has a negative trade balance with the rest of the world. In trade in services, India has a positive trade balance, whereas Germany has a negative trade balance.[7] In terms of the current account balance, despite the eurozone crisis, Germany has maintained a positive current account balance, which was $223.32 billion in 2012. Compared to this, India had a current account deficit - amounting to $60.04 billion in 2012.

[6] World Bank (2013a).

[7] UNCTAD Statistics on International Trade in services, available at *http://unctadstat.unctad.org/ReportFolders/reportFolders.aspx* (last accessed on January 22, 2014).

Table 1: Comparison of GDP and Per-capita GDP of India and Germany

Year	GDP, current prices ($Billions)		GDP per capita, current prices ($)		GDP (purchasing-power-parity - PPP) ($ Billion)		GDP(PPP) per capita ($ Billion)	
	India	Germany	India	Germany	India	Germany	India	Germany
2001	494	1883	471	22835	1723	2233	1644	27082
2002	524	2014	492	24398	1816	2268	1706	27475
2003	618	2428	572	29424	1997	2304	1849	27917
2004	722	2730	658	33090	2241	2399	2042	29079
2005	834	2771	749	33614	2518	2492	2260	30231
2006	949	2905	840	35297	2836	2669	2509	32419
2007	1238	3329	1081	40485	3196	2832	2789	34448
2008	1223	3641	1053	44398	3385	2911	2914	35497
2010	1365	3307	1159	40424	3701	2784	3141	34034
2011	1709	3311	1430	40496	4130	2926	3457	35797
2012	1880	3631	1553	45208	4491	3085	3708	38410
2013	1859	3428	1515	42569	4786	3167	3900	39335

Source: Extracted from World Economic Outlook Database, April 2014, IMF, available at http://www.imf.org/external/pubs/ft/weo/2014/01/weodata/index.aspx (last accessed on June 12, 2014).

As regards workforce, India's large workforce is more than 10 times that of Germany. In 2012, India had a workforce of 484 million compared to 42.5 million workers in Germany (Table 2). India's working age population (15-59 years) is expected to reach more than 900 million by 2030 (CRISIL, 2010). This young and growing workforce is an advantage for both the manufacturing and services sectors; it keeps the cost of production low, making India a favourable location for setting up business and manufacturing units. At the same time, skilled workers from India can contribute to the industry and services sectors in Germany.

Table 2: Labour force in India and Germany (in million)

Year	India	Germany
1990	330.7	37.3
2000	337.3	40.3
2005	464.5	41.3
2006	465.5	41.6
2007	466.8	41.9
2008	467.0	41.9
2009	467.7	42.0
2010	468.1	42.0
2011	476.6	42.5
2012	484.3	42.5

Source: Extracted from World Bank (2013a).

The above discussion shows that Indian and German economies complement each other in several ways. The growing middle class in India provides opportunities for German companies to invest in the market and cater to the Indian population. At the same time, India's large, skilled workforce complements the technological capabilities of German companies. German companies are also competent in providing infrastructure services, and India needs investments in sectors such as construction and logistics. India can become part of the global production networks of German companies, thereby enabling them to spread their risk. Access to the German market will help Indian companies cater to the wider EU market. Bilateral investment flows can help the Indian economy to develop its manufacturing facilities, lead to technological upgrading, diversify the research base, develop the organised services sector and reduce unemployment, while it can help German companies reduce costs, improve their global competitiveness and diversify their production networks. Hence, there are strong synergies between the two countries that are explored further in the paper.

3. Bilateral Investments between India and Germany

Foreign investors can invest in India through two routes - (i) automatic route[8] and (ii) approval route[9]. Unlike India, Germany does not have multiple entry routes. Foreign companies that are willing to invest in Germany come under the 'Foreign Trade and Payments Act, 1961' and the 'Regulation Implementing the Foreign Trade and Payments Act, 1986'. For companies that are at least 25 per cent owned by foreign holders, approval has to be sought from the Federal Ministry of Economics and Technology. To invest in Germany, a foreign business has to register the company or purchase shares in the existing company.

Table 3: Rank of Select Countries in Ease of Doing Business Index, 2013

Economy	Ease of Doing Business	Starting a Business	Dealing with Construction Permits	Getting Electricity	Registering Property	Getting Credit	Protecting Investors	Paying Taxes	Trading Across Borders	Enforcing Contracts	Resolving Insolvency
Singapore	1	4	2	5	36	12	2	5	1	12	2
Germany	20	106	14	2	81	23	100	72	13	5	19
China	91	151	181	114	44	70	100	122	68	19	82
Russia	112	101	178	184	46	104	117	64	162	11	53
Brazil	130	121	131	60	109	104	82	156	123	116	143
India	132	173	182	105	94	23	49	152	127	184	116

Source: World Bank (2013b).

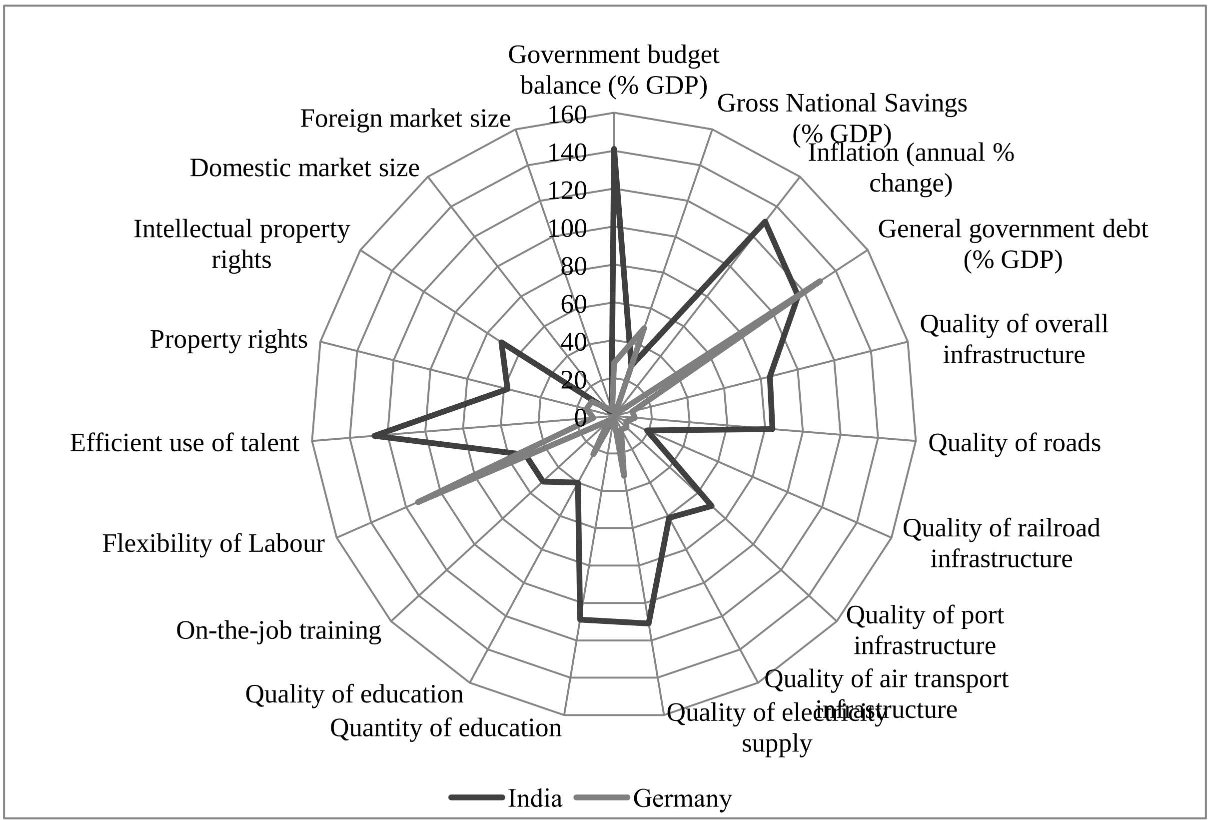
[8] Under the automatic route, no permission is required from the Government of India or the Reserve Bank of India (RBI).

[9] Under the approval route, approval is required from the Foreign Investment Promotion Board (FIPB) under the Department of Economic Affair, Ministry of Finance, Government of India.

As mentioned earlier, there are several factors that determine FDI inflows into a country. The ease of doing business in a country is one of the key factors. The Ease of Doing Business index by the World Bank ranks 186 economies in terms of their business operating environment and their regulations for foreign investments. Table 3 indicates that India and Germany ranked 20th and 132nd, respectively, in 2013.The table also shows that India has the lowest rank among BRIC (Brazil, Russia, India and China) countries largely due to its poor infrastructure, need for multiple clearances and quality of governance. The index is based on the perceptions of manufacturers and, therefore, indicates why India has not been able to do well in the manufacturing sector.

The Global Competitiveness Index of the World Economic Forum assesses comparative landscape of 148 economies. In 2013, Germany is ranked 4th in terms of national competitiveness. India is ranked 60th and lies much below other emerging economies such as China. The index is divided/broken in several sub-indices and India and Germany's comparative rankings on these are given in Figure 1.

Figure 1: Ranking of India and Germany on Selected Parameters of the Global Competitiveness Index in 2012



Source: Compiled from World Economic Forum (2013).

Note: The closer the rank to centre of the radar, higher is the ranking.

Compared to Germany, India has a lower rank on most parameters except gross national savings, general government debt, flexibility of labour and domestic market size. In all the other selected parameters, Germany performed better than India. Moreover on the Corruption

Perception Index[10] India was ranked 94th in 2013 which was much lower than Germany (12th) indicating a much higher level of corruption in India.

Despite the low rank on most other indicators, India's large, growing and unsaturated domestic market, economic reforms and liberalisation of FDI resulted in an increase in FDI inflows after 1991. India's global FDI inflows increased from $0.2 billion in 1990s to $31.5 billion in 2011 and $25.5 billion in 2012. Similarly, Germany's global FDI inflows reached to $48.5 billion in 2012 from $1 billion in 1990s. The per cent share in global FDI inflows of both countries also increased over time. Germany's share increased from 0.6 per cent in 1990 to 3 per cent in 2011, compared to India's share from 0.7 per cent to 2.2 per cent in the same years.[11]

Bilateral investment flows between India and Germany have also increased over time. As shown in Table 4, German investments in India have increased over time however they registered a sharp decline in 2012-13. According to statistics by the Department of Industrial Policy and Promotion (DIPP), German FDI inflows were valued at $123 million in 2000-01 and increased to $1,622 in 2011-12 and then declined to $860 million in 2012-13. Interestingly, there was a decline in overall into India in 2012-13 compared to the previous year and, therefore, the decline in investments is not unique to Germany (see Table 4).

Table 4: Trends in German Investment Inflows into India

Year	**Germany (in $ million)**	**All Countries (in $ million)**	**Per cent share in India's total FDI inflows**
2000-01	123.34	2,907.52	4.24
2001-02	113.48	4221.89	2.69
2002-03	143.91	3133.85	4.59
2003-04	81.17	2634.21	3.08
2004-05	145.35	3758.94	3.87
2005-06	302.85	5545.94	5.46
2006-07	119.95	15,726.19	0.76
2007-08	513.61	24,580.85	2.09
2008-09	629.22	27,330.82	2.30
2009-10	626.14	25,834.41	2.42
2010-11	199.74	19,426.90	1.03
2011-12	1621.95	36,504.00	4.44
2012-13	860.00	22,423.00	3.84
2013-14 (April-Sept)	538.00	11,376.00	4.73
Cumulative (April 2000 to September 2013)	**6,018.71**	**205,404.52**	**2.94**

Source: Extracted from DIPP, Government of India, FDI Statistics, various years.

Note: Data is given for the financial year starting in April and ending in March.

[10] E&Y and Transparency International (2014).

[11] Calculated from UNCTAD Database on 'Foreign Direct Investment', available at *http://unctadstat.unctad.org/ReportFolders/reportFolders.aspx* (last accessed on January 21, 2014).

Although German investments in India have declined in recent years, it is still large compared to other EU member countries such as France, Spain and Italy. Among the EU Member States, Germany is the fourth largest investor in India after the United Kingdom (UK), the Netherlands and Cyprus.[12] Overall, German investments since the year 2000 amounted to nearly $6 billion, accounting for a share of 2.9 per cent of total investments in India. Between April 2000 and September 2013, Germany was ranked 8th among foreign investors in India.[13] Between August 1991 and December 2009, Germany was second largest country for technological transfer (after the United States), with a share of 13.7 per cent in total technological approvals in India.[14] The top sectors of technology transfer from Germany are industrial machinery, electrical equipment including computer software and electronics, chemicals, mechanical and engineering and transportation.[15] These are also the sectors that can help India develop its manufacturing facilities and improve the quality of service delivery.

German investments in India are mainly concentrated in the automobile and chemical industry and the services sector (Table 5).

Table 5: FDI Equity Inflows from Germany by Sector (April 2012 to March 2013)

Sector	FDI inflow (in $ million)	Share in FDI inflows
Industry	**569.4**	**66.3**
Automobile industry	284.6	33.1
Chemicals (other than fertilisers)	108.8	12.7
Scientific instruments	62.1	7.2
Glass	46.4	5.4
Industrial machinery	44.2	5.1
Electrical equipment	6.1	0.7
Medical and surgical appliances	5.6	0.7
Agricultural machinery	3.8	0.4
Electronics	3.0	0.4
Metallurgical industries	2.5	0.3
Prime Movers (other than electrical generators)	2.3	0.3
Services	**269**	**31.3**
Services (including financial, banking, insurance, non-financial/ business, outsourcing, R&D, courier, tech. testing and analysis & others)	115.8	13.5
Trading	64.8	7.5
Energy (including power, petroleum and natural gas, and railway-related components)	39.1	4.5
Agriculture services	25.7	3.0
Construction development (including townships,	10.1	1.2

[12] The Netherlands and Cyprus are considered as tax havens due to their lower tax rates compared to other EU Member States and India.
[13] DIPP (2013a)
[14] DIPP (2010).
[15] DIPP (2010).

Sector	FDI inflow (in $ million)	Share in FDI inflows
housing, built-up infrastructure, etc.)		
Consultancy services	7.6	0.9
Computer software & hardware	5.9	0.7
Others	**21.2**	**2.4**
Total	**859.6**	**100**

Source: Extracted from Indo-German Chamber of Commerce (2013), Table 9, p. 115.

Today, several major German companies have a presence in India. German automobile giants such as Bayerische Motoren Werke AG (BMW) and Volkswagen Group have their manufacturing facilities and assembly plants in India. Several German small and medium enterprises (SMEs)[16] have also established operations in the Indian market. A German Centre has been established in the national capital region (NCR) by two German banks, viz., Bavarian Landesbank and Landesbank Baden Württemberg, to facilitate the activities of German SMEs in India. German companies prefer to set up their offices in Indian metro or Tier I cities.[17] A study of Indo-German Chamber of Commerce (2013) shows that about 25.4 per cent of the Germany companies were located in Mumbai followed by Bengaluru (14.1 per cent), Hyderabad (4.5 per cent) and New Delhi (4 per cent) between April 2012 and March 2013.

Economic growth and liberalisation of the OFDI regime facilitated global presence of Indian companies in different regions of the world. According to Reserve Bank of India (RBI) data, in 2008 Indian investments in Germany were valued at $81.5 million and in 2013 it increased to $131 million. Between July 2007 and December 2013, the consolidated investments by India in Germany were valued at $533.8 million. Among EU Member States, the Netherlands and the UK are preferred destinations for Indian investments and have received much higher investment flows than Germany (Table 6). One of the reasons for higher investments in the Netherlands and Cyprus is that these countries are tax havens.

Table 6: Indian Investments in Select EU Member States (in $ million)

EU Member States	2007 (July - Dec)	2008	2009	2010	2011	2012	2013	2007-2013
Netherlands	1179.0	993.8	1594.8	7937.4	2649.0	3963.1	7207.6	25524.7
UK	159.3	849.4	361.1	691.1	1675.0	1254.2	1647.0	6637.1

[16] Germany and India follow different definitions for characterizing SMEs. In Germany the category of micro, small and medium-sized enterprises (SMEs) is made up of enterprises, which employ more than 255 persons and which have an annual turnover not exceeding €50 million, and/or an annual balance sheet total not exceeding €43 million. In India, a micro enterprise is an enterprise where investment in plant and machinery does not exceed Rs. 2.5 million; a small enterprise is an enterprise where the investment in plant and machinery is more than Rs. 2.5 million but does not exceed Rs. 50 million; and a medium enterprise is an enterprise where the investment in plant and machinery is more than Rs. 50 million but does not exceed Rs.100 million.

[17] On the recommendations of the Sixth Central Pay Commission of India, Indian cities were classified as Tier I, Tier II and Tier III based on their House Rent Allowance. The Tier I cities or the metros have the highest House Rent Allowance in India. These cities include Bengaluru, Chennai, Delhi, Hyderabad, Kolkata and Mumbai.

EU Member States	2007 (July - Dec)	2008	2009	2010	2011	2012	2013	2007-2013
Cyprus	710.0	643.4	2527.0	444.8	647.3	333.0	321.1	5626.6
Denmark	314.2	283.9	81.2	150.1	92.9	117.1	1.6	1041.0
Luxembourg	4.6	1.7	1.5	7.4	90.5	395.4	38.6	539.7
Belgium	4.6	68.3	99.4	41.7	44.4	82.6	198.5	539.5
Germany	29.3	81.5	49.1	62.3	76.7	104.1	130.8	533.8
Spain	2.6	75.5	138.8	23.1	44.6	51.4	85.9	421.9
France	52.9	137.5	12.5	33.4	23.4	12.5	45.9	318.1
Italy	20.9	55.0	77.4	36.6	17.5	24.2	34.3	265.9
Czech Republic	20.7	17.5	18.8	7.1	82.2	19.0	1.1	166.4
Total EU	**2530.8**	**3220.1**	**5032.8**	**9446.4**	**5584.0**	**6444.0**	**9858.8**	**42116.9**

Source: Calculated from 'Data on Overseas Investments', RBI, *http://www.rbi.org.in/scripts/Data_Overseas_Investment.aspx* (last accessed on January 21, 2014).

Note: This table includes investments through automatic route, mergers and acquisitions, etc.

The majority of Indian investment in Germany is in the manufacturing sector. According to RBI data, between July 2007 and June 2013, 66.5 per cent of Indian investments were in the manufacturing sector and 30 per cent in services (Table 7). A study by Tiwari and Herstatt (2009) on Indian subsidiaries operating in Germany found that a large number of Indian companies are investing in sectors such as information technology (IT) and Information technology enabled services (ITeS), pharmaceuticals and automotive.

Table 7: Indian Investments in Germany by Sector (July 2007 to June 2013)

Sector	Consolidated Indian Investments in Germany (in $ million)	Per cent share in Consolidated Indian Total Investments
Manufacturing	334.1	66.50
Services	153.5	30.55
Financial, insurance, real estate and business services	129.0	25.67
Wholesale, retail trade, restaurants and hotels	18.1	3.60
Community, social and personal services	4.2	0.84
Transport, storage and communication services	2.2	0.44
Electricity, gas and water	14.8	2.95
Total	**502.4**	**100.00**

Source: Calculated from 'Data on Overseas Investments', RBI,

http://www.rbi.org.in/scripts/Data_Overseas_Investment.aspx (last accessed on January 21, 2014).

Note: This table includes investments through automatic route, mergers and acquisitions, etc.

A majority of the Indian companies in Germany are located in Hesse, which has the German national stock exchange (DAX) and the international airport at Frankfurt. Indian IT companies are largely located in this region. Other preferred locations include North-Rhein Westphalia and Baden.

Indian companies have started acquiring companies in Germany and, according to KPMG (2013), Germany is the third-largest among developed countries for investment through acquisition by Indian companies after the US and the UK. Between 2005 and 2012, of the 658 acquisitions, Indian companies made 43 acquisitions in Germany compared to 25 by China (KPMG, 2013). The major acquisitions are Dr. Reddy Laboratory's acquisition of Betapharm GmbH, the acquisition of Trevira GmbH by Reliance Industries Limited and Jeco Holding AG by Mahindra and Mahindra Limited.

The above analysis shows that overtime bilateral investments between India and Germany have grown. Given this, it would be interesting to look at the different bilateral agreements between India and Germany and understand their implication on bilateral investments.

4. Trade and Investment Agreements and their Implications

In the recent years there has been an increasing orientation towards trade and investment liberalization. This is evident from the increase in the number of RTAs and/or free trade agreements (FTAs). A principal reason for the rise of FTAs is the increasing perception that these arrangements promote trade liberalisation among the negotiating partners (Urata, 2002). Slow progress of the WTO negotiations and snowballing and domino effects as a result of which countries do not want to be left behind and political and strategic reasons are other reasons that have led to proliferation of FTAs.[18] The WTO allows its member countries to enter into RTAs through which they can trade among themselves using preferential tariffs and opt for easier market access conditions. Over the years, there has been an increase in the amount of global trade through the RTA route. There has also been a surge in investment agreements due to the WTO's failure to agree on direct investment issues.[19]

Investment flows can often be facilitated by robust inter-government agreements since such agreements offer operational certainty, investment protection and other benefits to investors from the contracting party, putting them in an advantageous position vis-à-vis the rest of the world. According to the United Nations Conference on Trade and Development (UNCTAD)[20], investment agreements are of different types – bilateral investment treaties (BITs) or bilateral investment promotion agreement (BIPA)[21]; double taxation treaties

[18] Between 1948 and 1994, the General Agreement on Tariffs and Trade (GATT) received 124 notifications of RTAs (related to trade in goods), and since 1995 more than 400 additional arrangements covering trade in goods or services have been notified. For details see *http://www.wto.org/english/tratop_e/region_e/regfac_e.htm* (last accessed on January 28, 2014).

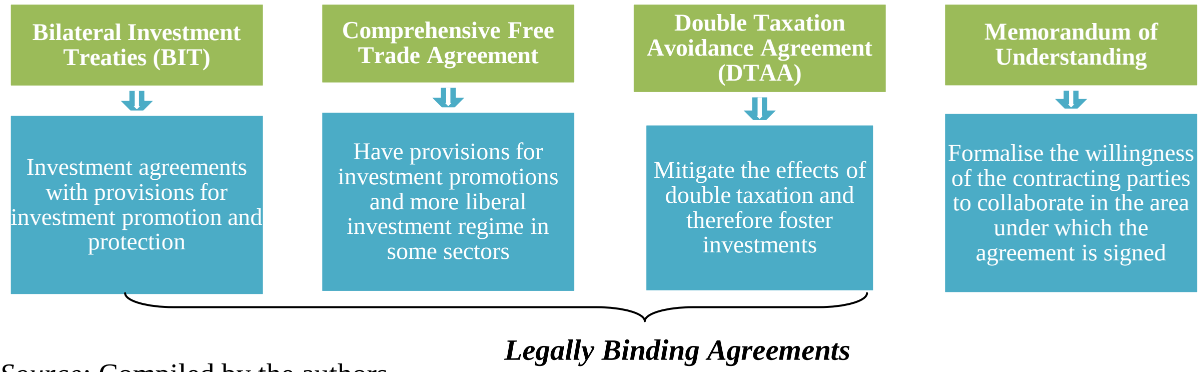
[19] The Fifth Ministerial Conference of WTO held in Cancun during September 10-14, 2003 failed to arrive at any agreement on several contentious issues including Multilateral Investment Agreements.

[20] *http://unctad.org/en/Pages/DIAE/International%20Investment%20Agreements%20(IIA)/Quantitative-data-on-bilateral-investment-treaties-and-double-taxation-treaties.aspx* (last accessed on July 10, 2014).

[21] BIT is a widely accepted term for investment treaties. However, it is termed differently by countries. For instance, India prefers to name it Bilateral Investment Promotion and Protection Agreement (BIPA), Canada prefers to name it Foreign Investment Protection and Promotion Agreement (FIPA) and Germany calls it BIT.

(DTTs)[22] and comprehensive regional trade agreements including comprehensive economic co-operation agreement (CECA), comprehensive economic partnership agreement (CEPA) and Memorandum of Understanding (MoU) between the government and other institutions (Figure 2).

Figure 2: Agreements that cover Investment



Source: Compiled by the authors.

India has a BIPA and a DTAA with Germany. As a member of the EU, Germany is now negotiating a Broad-based Trade and Investment Agreement with India, which is further likely to have an impact on bilateral investments between India and Germany. This section examines the present investment agreements between the two countries and analyses the scope of liberalising investments under the India-EU BTIA.

4.1 Bilateral Investment Treaties/Agreements

The UNCTAD defines BITs as '*international agreements signed between two countries for the reciprocal encouragement, promotion and protection of investments in each other's territories*'. Recent years have witnessed a sharp increase in the number of international agreements covering policies on FDI protection (Franck, 2007; Malik, 2006; Nziramasanga *et al.*, 2011). At the end of 2012, a total of 2,857 BITs had been concluded (UNCTAD, 2013).

By establishing the terms and conditions for private investment, BITs guarantee a 'level playing field' and certain standards of treatment that can be enforced through binding investor-to-state dispute settlement outside the domestic juridical system (Neumayer and Spess, 2005). Generally, BITs address four issues (Wong, 2006):

1. Conditions for the admission of foreign investors to the host State
2. Standards of treatment of foreign investors
3. Protection against expropriation
4. Methods for resolving investment disputes

[22] There are a multitude of different names for double taxation treaties such as double taxation agreement, capital tax treaties, tax treaties, or treaties covering the taxation of investment and income. India calls it as Double Taxation Avoidance Agreement (DTAA).

Germany concluded 127 BITs as of June 2013[23] and India has signed BIPAs with 83 countries of which 72 BIPAs are in force[24]. The BIPA between India and Germany was signed on July 10, 1995 and came into force in July 1998. In India, the Ministry of Finance is responsible for signing BIPAs, whereas in Germany BITs are signed by the Federal Foreign Office[25]. Architecturally, a BIT provides the scope, definition and coverage of the agreement and highlights the provisions in terms of admission and establishment, national treatment (NT), most favoured nation (MFN) treatment, expropriation and dispute settlement, among others. In certain cases, the extent of commitments under bilateral investment treaties may vary. For instance, BITs involving the US and Canada have a pre-establishment clause that allows potential investors to enter the domestic market of the host state with minimal or no regulations. Indian and German agreements largely do not have a pre-establishment clause. The architectural design of Indian and German bilateral investment treaties is given in Table 8.

Table 8: Substantive provisions in BIPAs/BITs of India and Germany

Provisions	**German Model (2008)**	**Indian Model (1991)**	**India-Germany BIPA (1998)**
Definition/coverage of Investment - Open List	Yes	Yes	Yes
Umbrella Clause	Yes	Yes	Yes
Post-Admission			
MFN	Yes	Yes	Yes
NT	Yes	Yes	Yes
Investment Protection			
Standards of treatment	Yes	Yes	Yes
Transfers	Yes	Yes	Yes
Expropriation			
Direct	Yes	Yes	Yes
Indirect	Yes	Yes	Yes
Key personnel	Yes	Yes	Yes
Exceptions			
Economic Integration Agreements	Yes	No	Yes
General exceptions	Yes	No	Yes
Security interests	No	No	Yes
Taxation	Yes	No	Yes

Source: Compiled from OECD (2006), Table 6.2, p. 147; Indian Model Text of BIPA, available at Department of Economic Affairs, Ministry of Finance, Government of India, http://finmin.nic.in/the_ministry/dept_eco_affairs/icsection/Indian%20Model%20Text%20BIPA.asp (last accessed on March 31, 2014).

[23] For details, see UNCTAD, *http://unctad.org/Sections/dite_pcbb/docs/bits_germany.pdf* (last accessed on January 10, 2014.)

[24] For details, see Ministry of Finance, Government of India, *http://finmin.nic.in/bipa/bipa_index.asp?pageid=1* (last accessed on January 10, 2014.)

[25] *http://www.auswaertiges-amt.de/EN/AAmt/Uebersicht_Navi.html* (last accessed on January 2, 2014).

In terms of architectural design, the Indian and German agreements are similar. Both have an Umbrella Clause that creates a legal obligation by requiring a state to observe commitments it may have entered into with investors of the other contracting state. Apart from talking about favourable investment conditions and treatment, the Umbrella Clause in the India-Germany BIPA has a provision where neither party can place any constraints on the international movement of goods or persons directly connected with an investment being transported subject to bilateral or international agreements, thereby ensuring a broad coverage (Tan, 2012). In many cases, foreign investors have issued notices to the Indian Government invoking provisions under the BIPAs signed by India. There are several disputes also such as that in the case of Vodafone India that tried settling its tax disputes using India-Netherlands BIPA (signed in November 1995 and came into force in December 1996).[26]

As regards admission and establishment of investments, international law does not bind any nation to admit foreign investment. FDI is in the territorial jurisdiction of each country and can be liberalised autonomously, unless bound under a trade agreement such as the India-EU BTIA. Each government determines whether to admit a foreign investor and it can also decide the terms and conditions for admission and establishment.

Although the provisions of both NT and MFN are included in the Germany-India BIPA, it makes an exception for investors of third States on account of its membership of, or association with, a customs or economic union, a common market or a free trade area. This implies that in the case of Germany, it can accord more favourable treatment to EU Member States. Interestingly, the Germany-Singapore Investment Treaty signed in 1973 does not make this exception. The India-Germany BIPA also accords fair and equitable treatment and full protection and security to investments and investors and has provisions on direct and indirect expropriation.

In a nutshell, the India-Germany BIPA as it stands today encompasses all provisions for protection of investors and investments in each other's markets. This legally binding document highlights the obligations of each contracting party towards investors and investments from the other contracting party. However, while the agreement highlights general obligations, it does not make any specific liberalisation commitment.

4.2 Double Taxation Treaties (DTTs)

Bilateral double taxation treaties (DTTs) have become very popular in recent years with over 2,289 treaties in place at the end of 2008 (Parikh, *et. al*, 2011). There are two architectural designs -, the OECD model[27] and the UN model[28] that are used for defining and formulating DTTs. Among these, the OECD model is widely used and followed. The purpose of DTTs is not only to avoid double taxation but also pave a way for the exchange of financial and tax

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[26] *http://articles.economictimes.indiatimes.com/2014-02-23/news/47603866_1_vodafone-india-services-vodafone-international-holdings-bv-india-netherlands-bipa* (last accessed on July 10, 2014).

[27] For details, see *http://www.oecd.org/tax/treaties/oecdmtcavailableproducts.htm* (last accessed on July 10, 2014).

[28] *http://www.un.org/en/development/desa/publications/double-taxation-convention.html* (last accessed on July 10, 2014).

information between the contracting parties. Generally, the stated objective of bilateral tax treaties is to prevent the burden of double taxation on residents of one country as well as prevent tax evasion by residents of one country when they earn income in another country (Parikh, *et. al*., 2011).

DTTs serve to standardise taxable income definitions, and identify the jurisdiction of the taxation authorities among the contracting parties. In particular, they are useful in clarifying actual income taxability and reducing related ambiguities. Some treaty provisions might conflict with domestic tax laws, curtailing national fiscal sovereignty. On the controversial side, DTTs help in exchange of tax information between tax authorities (Parikh, *et. al*., 2011).

DTT are legally binding bilateral agreements covering taxes on income imposed on behalf of each Contracting State. When a taxpayer is resident in one country but has a source of income in another country, it may give rise to double taxation if the income is repatriated. This is primarily governed by two rules:

- Source of Income: When income is earned in the source country, the jurisdiction of that country applies tax on the income originated irrespective of whether the income accrues to a resident or a non-resident;

- Residence of Income: This mandates that power to tax should rest with the country in which the taxpayer resides.

If both rules apply simultaneously to a business entity and it were to suffer tax at both ends, the cost of operating on an international scale would become prohibitive and deter the process of globalisation. To avoid that problem, the DTTs become important. The DTT is, in effect, a bilateral agreement between two countries that aims at mitigating the incidence of double taxation, thereby promoting and fostering economic trade and investment between two countries. DTTs can be comprehensive agreements covering all sectors and entities or limited agreements covering only certain sectors. As of June 2011, Germany concluded 91 DTTs[29]; and India has DTAAs with 88 countries of which 85 DTAA are in force.[30] The DTAA between India and Germany is a comprehensive one, signed on June 19, 1995 and came into force on October 26, 1996 with respect to taxes on income and capital.[31]

4.3 Bilateral Co-operation and Collaboration between India and Germany

India and Germany have had a strategic partnership since 2000 and has been further strengthened with the first Intergovernmental Consultations (IGC) held in New Delhi in May 2011. The two countries have several institutionalised arrangements to discuss bilateral and global issues of interest, etc. The two countries signed Science and Technology (S&T)

[29] *http://unctad.org/en/Pages/DIAE/International%20Investment%20Agreements%20(IIA)/Country-specific-Lists-of-DTTs.aspx* (last accessed on July 11, 2014).
[30] *http://pib.nic.in/newsite/erelease.aspx?relid=93330* (last accessed on July 11, 2014).
[31] The full text of the agreement is available at *http://law.incometaxindia.gov.in/DIT/File_opener.aspx?fn=http://law.incometaxindia.gov.in/Directtaxlaws/cbdt/dta/A1_Germany.htm* (last accessed on January 6, 2014).

Agreements in 1971 and 1974. At present, there are more than 150 joint S&T research projects and 70 direct partnerships between Indian and German universities.

Indo-German co-operation in trade and technology is one of the most dynamic facets of the bilateral partnership. There is a Joint Commission on Industrial and Economic Co-operation led by the Finance Minister on the Indian side, and the Economics Minister on the German side. In addition, there are seven Joint Working Groups in sectors including agriculture, automobile, infrastructure, energy, coal, tourism and vocational education. Forums such as the Indo-German Energy Forum focus on specific issues such as renewable energy, energy-efficient technologies and alternative fuels.

There are several MoUs between India and Germany. These are inter-government or between industry bodies or between industry and the government. There are also MOUs between companies from both countries. Examples of inter-government MoUs include the agreement between Ministry of Human Resource (India) and Federal Minister of Education and Research (Germany) to facilitate student exchange programmes. Inter-industry MoUs include an agreement between Infosys Ltd (India) and Bertelsmann Stiftung (Germany) to support vocational education and training in India. MoUs between the government and industry include an agreement between DB Systel (Germany) and Centre for Railway Information Systems (India) in the field of information systems related to railways. The Solar Energy Centre, Ministry of New and Renewable Energy, Government of India and Fraunhofer Institute for Solar Energy Systems (Germany) have a MoU to promote co-operation in solar energy. Industry associations have also been involved in strengthening relations between India and Germany. For example, the Federation of Indian Chamber of Commerce and Industry (FICCI) has various MoUs with German companies. These MoUs facilitate collaboration and joint work but they do not have a legal standing.

4.4 Provisions for Investment under Comprehensive FTAs

Besides BITs, DTAAs and other collaborations, comprehensive bilateral FTAs (such as CECA and CEPA) also have provisions on investment promotion and protection. These comprehensive agreements play a significant role in increasing FDI flows by legally binding the host country to provide assurance to investors as well as taking commitments in specific sectors that often go beyond the autonomous FDI regime of the contracting parties (this is also known as forward-looking commitments to liberalise FDI). In this way, free trade agreements go beyond the scope of all other bilateral investment agreements between the contracting parties.

In most cases, if countries have a bilateral investment treaty with a trading partner, the provisions of existing BIT get included in the 'Investment Chapter' of the comprehensive FTAs. However, they may also include clauses that go beyond the standard BIT template as well as the WTO commitments of the countries. A study by Horn *et al.* (2009) indicates that the Preferential Trade Agreements (PTAs) signed by the EU or the US go beyond the coverage of regulatory issues, by including provisions in areas that are not currently covered by the WTO agreements at all, such as investment protection, competition policy, labour standards and protection of the environment.

Most comprehensive agreements can have dual coverage of investments, especially for the services sectors; while there is a separate 'Investment' Chapter, investments in services sectors are covered through Mode 3 (commercial presence) in the 'Trade in Services' Chapter. However, there is also a provision built in the trade agreement about which chapter prevails. Such dual coverage has been seen in India's trade agreements such as India-Singapore CECA and India-Korea CEPA. The on-going India-EU BTIA is a comprehensive trade agreement covering trade in goods, trade in services, investment, intellectual property rights, competition policy, customs and trade facilitation, government procurement and sustainable development issues, among others[32]. If signed, this agreement will supersede the bilateral investment agreements that India has with individual EU Member States and will be the most comprehensive agreement.

It is also important to note that the status of the India and Germany BIPA or any other bilateral agreement is likely to change after the India-EU BTIA is signed. In 2009, the EU signed the Lisbon Treaty, which states that the EU will negotiate new trade agreements and individual member countries (including Germany) will not be able to negotiate future trade agreement on their own with their respective trading partners. However, the trade agreements from before 2009, which member countries have, will be valid until the EU negotiates a trade agreement with the respective partner country.[33] This is also true of investment agreements. In fact, individual EU member countries' BIPAs or BITs with other countries such as India prior to 2009 will be valid as long as the EU does not have a trade agreement with those countries. After 2009, if the European Commission negotiates new BITs with third countries including India, it will overrule the existing BIPAs that India has with select EU Member States including the UK, Netherlands, France and Spain.[34] Moreover investment is a key component of the India-EU BTIA. Thus, the India-EU BTIA or any investment agreement that India signs with the EU can overrule India-Germany BIPA. While this takes away the advantage that Germany has today *vis-à-vis* other EU members who do not have BIPA with India, the new investment agreement has to be more robust that the existing bilateral agreement between India and Germany.

The above sections highlight the trends and patterns in investments in India and Germany, based on secondary information analysis. The data reflects the present volume of FDI Inflows and outflows, areas of investment and the comparative position of India and Germany in each other's global investments. An analysis of investment agreements highlight that bilateral investments can be strengthened through a robust institutional mechanism and bilateral agreements. In order to understand future prospects and barriers to enhancing bilateral investments between the two countries, a primary survey was conducted by the Indian

[32] India-EU BTIA negotiations are in their final leg: Anand Sharma Government Invites Poland companies to invest in the infrastructure sector. Press Information Bureau, Government of India. July 11, 2011. *http://pib.nic.in/newsite/erelease.aspx?relid=73130*

[33] For details, see European Commission (2012).

[34] *http://www.finmin.nic.in/bipa/bipa_index.asp?pageid=2* (last accessed on July 10, 2014).

Council for Research on International Economic Relations (ICRIER), which is discussed in next section.

5. A Primary Survey: Prospects and Challenges in Enhancing Investments between India and Germany

A primary survey was conducted in India and Germany. It included stakeholder's consultation, in-depth one-on-one interviews and an online survey. This was conducted in four phases. In the first phase, a preliminary survey was conducted through a webinar in which both Indian and German companies participated. In the second phase, a stakeholder's consultation was conducted in Chennai (Tamil Nadu) to gather the views of German companies in India and Indian companies that have a presence in Germany. In addition, in-depth interviews were held in Delhi, Mumbai, Chennai and Bengaluru with German and Indian companies that have a presence in each other's market. In the third phase, in-depth interviews were conducted in Frankfurt and Köln in Germany with companies, government bodies and associations to identify prospects and problems in each other's market. Field visits were made to factory sites to understand the size and operations of Indian companies in Germany. In parallel, as a fourth phase, an online questionnaire was circulated to members of the Indo-German Chamber of Commerce , which included separate questionnaires for Indian and German companies. The primary survey was based on a semi-structured questionnaire, with some open-ended questions to get more information. Care was taken to cover companies across different sectors. The sampling frame is given in Table 9.

Table 9: Sampling Frame

Profile of Respondents	Number of Respondents
Indian Companies	132
German Companies	187
Indian Associations	2
German Associations	2
Academics and sectoral experts	4
Central ministries	2
Embassies	2
Total Number	**331**

German companies were asked about their mode of entry in India, their economic activity and their preferred location in the Indian market. The companies from both countries were then asked about their perceptions on the two markets—their reasons for establishing operations and their views on the operating environment. To better understand the problems, Indian and German companies were asked about the barriers they faced in each other's market and the ease of doing business in India and Germany. Finally, questions were asked about future prospects and the potential for investing in India and Germany. The following sections present the survey findings.

5.1 Sample Distribution

5.1.1 German Companies in India

The majority of German companies (80.7 per cent) have entered India through the automatic route (Table 10). Of these, around 96.3 per cent have established a wholly-owned subsidiary in India while the remainder have set up a joint venture with an Indian partner. Some German companies pointed out that they wanted full control over their operations and technology transfer; therefore, they prefer the wholly-owned subsidiary route rather than a joint venture with an Indian company.

Table 10: Route of Entry of German Companies in India

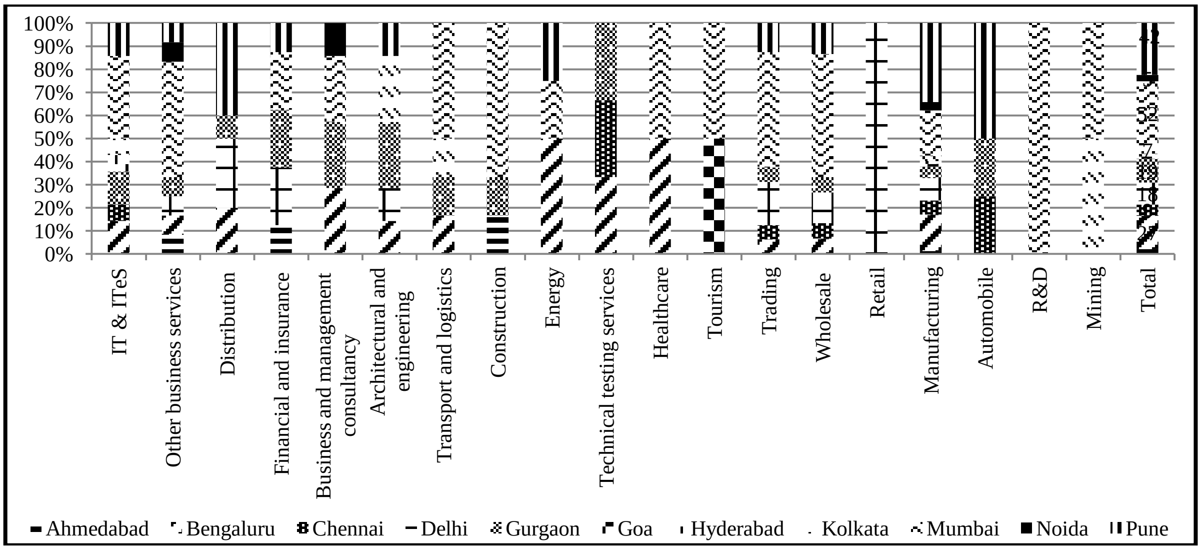
Mode of Operation	Number of Companies	Per cent Share
Automatic route	151	80.7
SIA/FIPB or government route	11	5.9
Mergers and acquisition	25	13.4
Total number	**187**	**100.0**

Source: Primary survey.

Unlike China, where Germans have largely invested in the manufacturing sector, in India German companies have mainly invested in the services sector. Of the 187 companies, 97 have invested in the services sector (51.9 per cent) and 82 in manufacturing (43.9 per cent). Within the services sector, IT and ITeS has the majority of German companies.

Mumbai is the preferred location for German companies, with 52 per cent having offices in Mumbai followed by Pune (42 per cent) and Bengaluru (27 per cent). In terms of sectors, the majority of the manufacturing companies are in Pune, transport and logistics companies and construction companies are in Mumbai, tourism is in Goa and mining is in Kolkata (Figure 3).

Figure 3: Sectoral and Spatial Distribution of German Companies in India



Source: Primary survey.

The survey found that the German companies in India are aware of the growth prospects and are investing in developing end-to-end infrastructure in the Indian market. Companies are also working with smaller enterprises to foster overall growth of the Indian economy. The case of a German company in distribution services is given in Box 1.

Box 1: Metro Cash & Carry – India Operations

The first Metro Cash & Carry centre in India opened in Bengaluru in 2003 and at present there are 15 wholesale centres, including two each in Bengaluru, Hyderabad and Mumbai, and one each in Jaipur, Ludhiana, Jalandhar, Amritsar, Delhi, Kolkata, Vijayawada, Indore and Zirakpur. Metro Cash & Carry started its presence in bigger cities and then opened smaller stores in Tier II and Tier III cities. The stores stock only a few categories of products. Metro Cash & Carry sources 95 per cent of its products locally. In India it has joined hands with various government agencies; it has an agreement with the Punjab Agro Industries Corporation and has set up agriculture sourcing platforms—'farmers' collection centres'—in Karnataka, Andhra Pradesh, Punjab, Maharashtra and West Bengal. Metro has its own distribution channel and logistics solution in India. Due to its business-to-business operating model, Metro is doing well even in states such as West Bengal where the state government is opposed to FDI in retail. In West Bengal, small retailers are the largest buyers from Metro Cash & Carry stores. According to an estimate, in 2012 Metro generated revenue of $492 million (€355 million) from India, which is around one per cent of the company's global revenue.

Source: http://www.metro.co.in/public/home; http://www.smartinvestor.in/market/Compnews-206578-Compnewsdet-Metro_Cash_amp_Carry_revamps_India_strategy.htm (last accessed on May 14, 2014).

Overall, the primary survey findings were in consensus with the secondary information. The survey reiterated that German companies have an investment interest in the services sector in India and largely opt for the automatic route to avoid regulatory problems.

5.1.2 Indian Companies in Germany

The majority of Indian companies (72 per cent) have established a wholly-owned subsidiary in Germany, 21.2 per cent merged or acquired German companies to establish their operations in the region and the remainder are present through joint ventures. Wholly-owned subsidiaries in Germany receive the same benefits as any other EU company. The experience of an Indian company established in Germany as a wholly owned subsidiary is given in Box 2.

Box 2: Shalimar Food GmbH

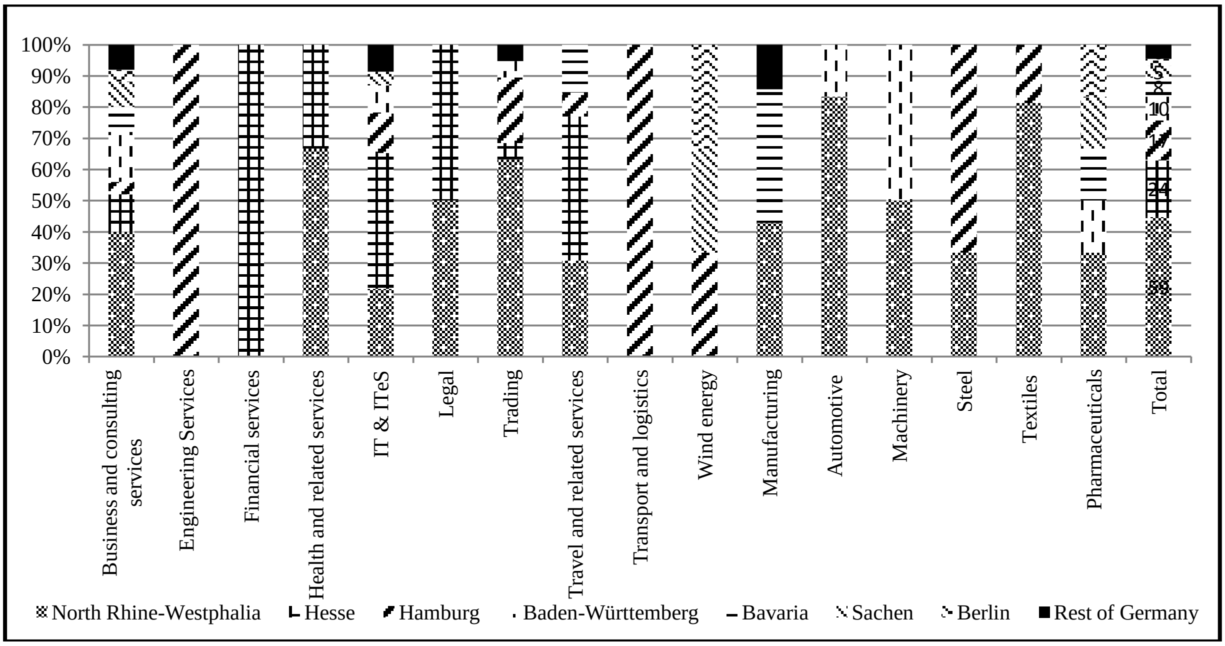
The company is a wholly-owned subsidiary of an Indian company called Shalimar Food Private Limited that was established more than 30 years ago. The company is owned by an Indian who has been living in Germany for more than three decades and has German citizenship. In Germany it has a state-of-the-art manufacturing and packaging facility in Köln and the product range includes more than 1,000 different products for Italian, Indian, Mexican and Chinese cuisine. While the top-level management of the company constitutes Indians with German citizenship and knowledge of the language, it also employs Germans. It largely sources its products from Italy, including some traditional Indian products, as the products are better quality and import procedures are simpler. Germany has a mix of cultural ethnicities and, therefore, there is a huge market and growth potential in the imported and packaged food segment. The company is fully satisfied with its operations in

Germany and the operating environment and regulatory structure. The company forecast the future growth rate to be at least 25 per cent and, keeping in view the growth prospects, the company has acquired another space to set up a branch.

Source: Primary survey

The sector-wise spatial distribution of Indian companies in Germany is given in Figure 4. Most Indian companies are located in the western region of North Rhein-Westphalia (59 per cent), while Hesse (24 per cent) and Hamburg (17 per cent) also have high concentrations of Indian companies. Real estate prices have a bearing on the choice of location for a company; there are variations in real estate costs across different cities, with Frankfurt and Munich being the most expensive locations.

Figure 4: Sectoral and Spatial Distribution of Indian Companies in Germany



Source: Primary survey.

North Rhein-Westphalia is the preferred location for healthcare services, automobile sector, trading and textiles because of its proximity to the Netherlands. Hesse has a large number of financial service providers and IT companies, while transport and logistics companies and engineering service providers are concentrated in Hamburg.

5.2 Overall Perceptions of Respondents

The survey participants were asked for their views on issues that affect trade and investments between India and Germany. These include the present agreements, tax and investment regime in each other's markets and future prospects. Open-ended questions were asked and, therefore, the responses were descriptive.

5.2.1 Perceptions of German Companies

Most German companies consider India as an attractive investment destination due to the large and growing market. In addition, technology penetration is low in India and, therefore, there is huge untapped potential for companies to invest in the country. Within the country, several factors are considered when selecting the investment location. These include infrastructure connectivity, cost of establishment, market size, manpower availability, consumer preference, and knowledge of English language and manpower availability. German companies pointed out that India has a huge/large market size, has availability of manpower at competitive prices, and potential to grow, all these factors attracts them to invest into India. They do not consider incentives offered/given by the Indian government as an attraction for investments. For example, some of the incentives given by India, especially those linked to exports, can be actionable under the Subsidies and Countervailing Agreement of the WTO and, therefore, German companies do not consider them attractive. When asked about the Indian Special Economic Zone (SEZ) policy, most German companies said that they do not have any operations in SEZs since the regulations change frequently. Moreover, there is no support from the Department of Commerce, under the Ministry of Commerce and Industry in infrastructure development and there is a negative feeling in India through the media about SEZs. The lack of co-ordination between the centre, the state and the Development Commissioner's office has made it difficult for units to locate in SEZs. Moreover, several SEZs do not have basic facilities such as waste disposal facilities. In general, German companies found the National Manufacturing Policy to be more focused than the SEZ policy. They said that the government has identified 12 national manufacturing zones and similarly there should have been a limit on the number of SEZs. However, it may be difficult to acquire land for the zones, especially contiguous land. German companies also pointed out that India should have a clear vision to develop manufacturing and production networks and economic corridors. Foreign companies are willing to invest in India if they are given conducive investment environment.

German Companies considered some of the states such as Gujarat, Maharashtra, Tamil Nadu and Goa as investor-friendly. They pointed out that the state policies should be growth-driven and aim to generate employment. Most companies reported stable revenue growth in India with India's market share to be around 5-10 per cent of their global market. Companies expressed satisfaction with the fact that even during the global slowdown their revenue from the Indian market did not decline significantly.

In terms of employment, German companies said that they do not face any problems. Most German companies employ Indian nationals/locals and not German staff, as it would increase their costs. At the outset companies face minor hurdles due to differences in work culture, but after being trained, the employees' performance is satisfactory. It was also pointed out that Indian staff is enthusiastic and eager to learn.

German companies highlighted macro-economic and political instability in the Indian market. In the past few years India has faced a slight slowdown in growth rates and experienced high inflation. This has affected demand and the business of German companies in India. Political instability leads to policy uncertainty, which affects existing businesses as well as the will of other companies interested in the Indian market. For instance, in the case of FDI in multi-brand retail, states have been given the right to reject or allow multi-brand retailers. This has led to uncertainty, as companies are unsure if with a change in government the policy can be changed for each state.

While companies are aware of the India-Germany BIPA and the DTAA and also use these two, the level of knowledge about the India-EU BTIA is still very low. Companies were hardly aware of the benefits that the India-EU BTIA might bring and they said that there is limited engagement of industry in the negotiation process. As a result, the companies did not have major suggestions on the agreement or were not very aware of its likely outcomes. In India, German companies are engaged in government contracts, which they receive either through competitive bidding or through their partners. The companies stressed that that it would increase transparency in government procurement if India became part of the WTO's Plurilateral Government Procurement Agreement. Companies engaged in infrastructure projects would like government procurement to be part of the India-EU BTIA.

5.2.2 Perception of Indian Companies

The majority of Indian companies said that Germany is a large market in Europe, which is well protected by law; and the incidence of corruption and bribes is much lower than in India. The country has well-developed infrastructure and a strong research and development (R&D) base. Some respondents pointed out that they have been operating in Germany for a long time because of which they have established their operations and supply chain not only in the country but also across Europe. Within Germany, companies decide their location based on cost, assistance from the government and connectivity with other locations. Indian companies in Germany are less globalised than Germany companies in India. Unlike German companies that prefer to engage in competitive bidding for projects, Indian companies largely work with close associates and acquire information about projects through word-of-mouth or through trusted contacts. Their market share is largely concentrated in Germany with around 20-50 per cent share in the total revenue; the rest of the business comes from other countries in Europe. Interestingly, most Indian companies pointed out that they did not suffer from the global slowdown as they are in the business of specialised products such as Indian food products or in providing IT services or in a specific technology.

The companies pointed out that there is a local employment condition in Germany and in any case, companies have to hire Germans for legal and technical support. It was also pointed out the Germans are employed for managerial positions which helps to get business. Companies were satisfied with the available skills; however, they mentioned that labour laws in Germany are very strong and cumbersome and sometimes it poses a problem for them. Labour unions are more active in Germany than in India; and they regulate the salaries and grading of employees. Worker's Councils regulate work timings.

Indian companies are more aware of the India-Germany BIPA and DTAA, but they hardly understood the concept and function of the India-EU BTIA. Most companies pointed out that businesses should be given adequate knowledge about the India-EU BTIA and this would enable them to understand its costs and benefits

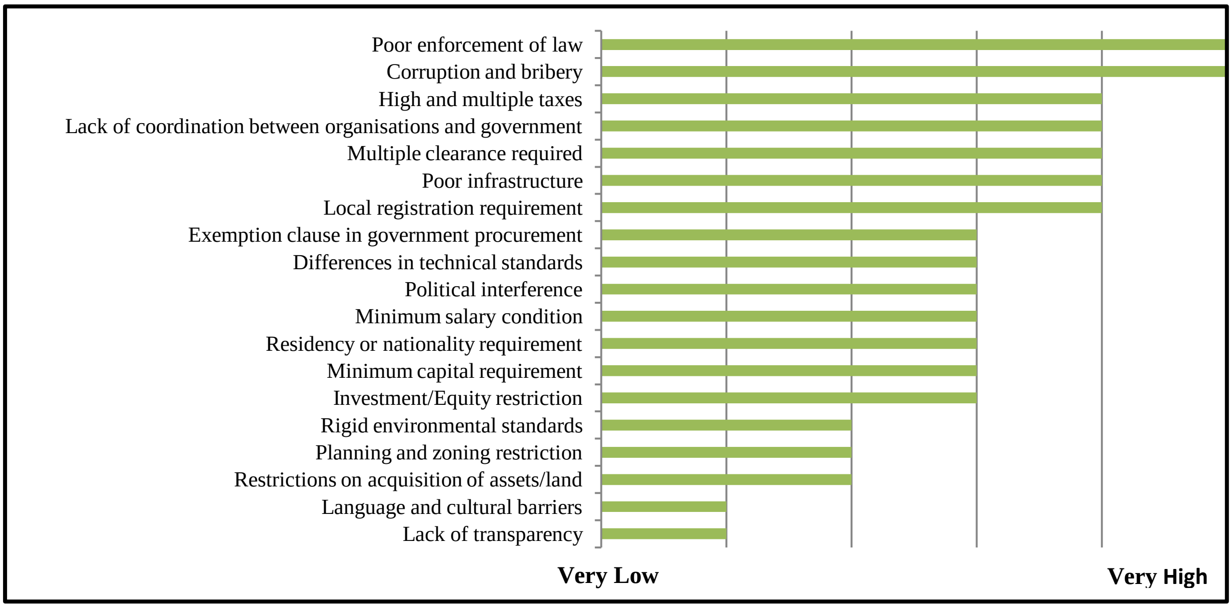
5.3 Perceptions about Barriers to Bilateral Investments

To understand perceptions about barriers, we created a severity index[35]. Survey participants were given a list of potential barriers and asked to rank their impact on the business as 'very high', 'high', 'normal', 'low' and 'very low'. Based on the responses, the frequency of the rank for each barrier was calculated and the rank receiving the highest frequency (mode) was assigned to the barrier. The barriers were then ranked.

Participants also elaborated on some barriers, which are included below.

5.3.1 Barriers faced by German Companies in India

Figure 5: Severity of Barriers for German Companies



Source: Primary survey

The participants elaborated on some of these barriers.

- *Corruption and bribery.* While most German companies face this barrier in India, in Germany bribery is an offence under the law, since Germany follows the anti-bribery convention. If a German company makes informal payments, it faces a legal trial in Germany.
- *Poor law enforcement.* Although India has laws in place, their enforcement is weak, which leads to operational uncertainty. Some German respondents said that the application of law is subject to interpretation by individual government officials and therefore, they often face new issues. Most German companies fear that the Indian

[35] Leonidas (1995).

courts cannot do much to resolve an issue and there are delays. In general, majority of German companies expressed low faith in the Indian legal system.

- *Issues related to taxation.* Even though basic tax rates are higher in Germany than in India, the overall tax burden is greater in India due to the multiplicity of taxes. In India the highest income tax rate is 33 per cent compared to 45 per cent in Germany[36], but the corporate tax rate is 29.5 per cent in Germany and 33.9 per cent in India[37]. Moreover, companies have to pay several state taxes and duties if they want to establish a pan-India presence. Companies have to pay corporate tax, capital gains tax, dividend tax, etc., which leads to a high tax burden. It was also pointed out that tax policy decisions are taken without industry consultation and certain exemptions such as the Minimum Alternative Tax (MAT) exemption, are withdrawn without a discussion with the stakeholders. In addition, the transfer price policy of India is narrowly defined, which undermines genuine foreign transactions. For instance, transfer pricing of intra-group financial arrangements such as loans and guarantees has led to major controversies. Some of these financial arrangements do not come under the purview of transfer pricing in other countries. In addition, taxes are imposed spontaneously in India, such as the retrospective tax policy, which adds to operational uncertainty. German companies also pointed out that they face difficulties in realising refund of duties from India.

- *Profit repatriation.* While salaries earned in India can be transferred to the home country, dividends earned by the foreign owner can only be transferred when closing operations and after paying taxes on them. As per the India-Germany DTTA, dividends may be taxed in both countries, with some exceptions. As a result, some German participants pointed out that they reinvest the dividends, but it is not their preferred option.

- *Infrastructure Bottlenecks.* Manufacturing facilities in India are poor and located in remote places with poor road and port connectivity. This is true even of SEZs and industrial clusters. Even if companies locate in states with major ports, the roads connecting the ports are not well developed, leading to losses and pilferage during transportation. Storage and warehousing facilities in India are inadequate and most companies have to invest in these facilities. German companies such as Deutsche Post (DHL Express) have used this as an opportunity to invest in logistics services; however, they are unable to operate in verticals such as the processed food supply chain due to lack of supporting infrastructure in India.

On getting market information, majority of German companies said that there are very few reliable sources. There is no website that provides consolidated information. Companies also find it difficult to identify a reliable Indian partner that has a huge investment capacity and

[36] Extracted from Table: Individual income tax rates between 2006 and 2013, *http://www.kpmg.com/Global/en/services/Tax/tax-tools-and-resources/Pages/individual-income-tax-rates-table.aspx* (last accessed on February 2, 2014).
[37] Extracted from Table: Global corporate tax rates between 2006 and 2013, *http://www.kpmg.com/Global/en/services/Tax/tax-tools-and-resources/Pages/corporate-tax-rates-table.aspx* (last accessed on February 2, 2014).

similar business interest. Some companies mentioned that a decade ago it was easier to work with Indians; however, Indian entrepreneurs have become arrogant, which makes it difficult to work with them

Second, even though India has progressively liberalised its FDI regime, it is still restrictive and several conditions are imposed on foreign companies. According to Organisation for Economic Co-operation and Development (OECD)'s FDI Regulatory Restrictive Index, 2013, India has the sixth most restrictive FDI regime after China, Myanmar, Saudi Arabia, Indonesia and Jordon, among 58 countries.[38]

In India, FDI restrictions vary across sectors (Table 11). In several sectors where full foreign presence is allowed, it is subject to minimum capital requirements and other restrictions. For example, in construction and related engineering services, there is a minimum capital requirement of $10 million for wholly-owned subsidiaries and $5 million for joint ventures with Indian partners; and a minimum lock-in period of three years (from the completion of minimum capitalisation before original investment) for repatriation of the amount. Unlike services, most of the manufacturing sector is open to foreign investment but there are investment restrictions in the agriculture sector. FDI is prohibited in sectors like railways, manufacture of cigars, cheroots, cigarillos and cigarettes, of tobacco, etc., *Nidhi* companies and atomic energy.

Table 11: FDI Limits in Sectors in India

FDI Limit	Sectors	Route
74%	➢ Broadcasting carriage services including teleports, direct-to-home, multiple system cable networks, mobile TV and headend-in-the-sky (HITS) ➢ Air transport services (non-scheduled air transport service) ➢ Ground handling services ➢ Banking private sector	Up to 49 percent through automatic route; beyond 49 percent through government route
	➢ Satellites – establishment and operation	Government route
51%	Multi-brand retail trade	Government route
49%	➢ Cable networks (local cable operators) ➢ Petroleum refining by public sector undertakings (PSUs) ➢ Air transport services- domestic scheduled passenger airline	Automatic route
	Private security agencies	Government route
26%	Insurance	Automatic route
	➢ Defence industry ➢ Broadcasting services (terrestrial broadcasting FM radio and uplinking of news and current affairs TV channels) ➢ Print media (publishing of newspapers and periodicals dealing with news and current affairs and publication of Indian editions of foreign magazines dealing with news and current affairs) ➢ Banking services – public sector	Government route

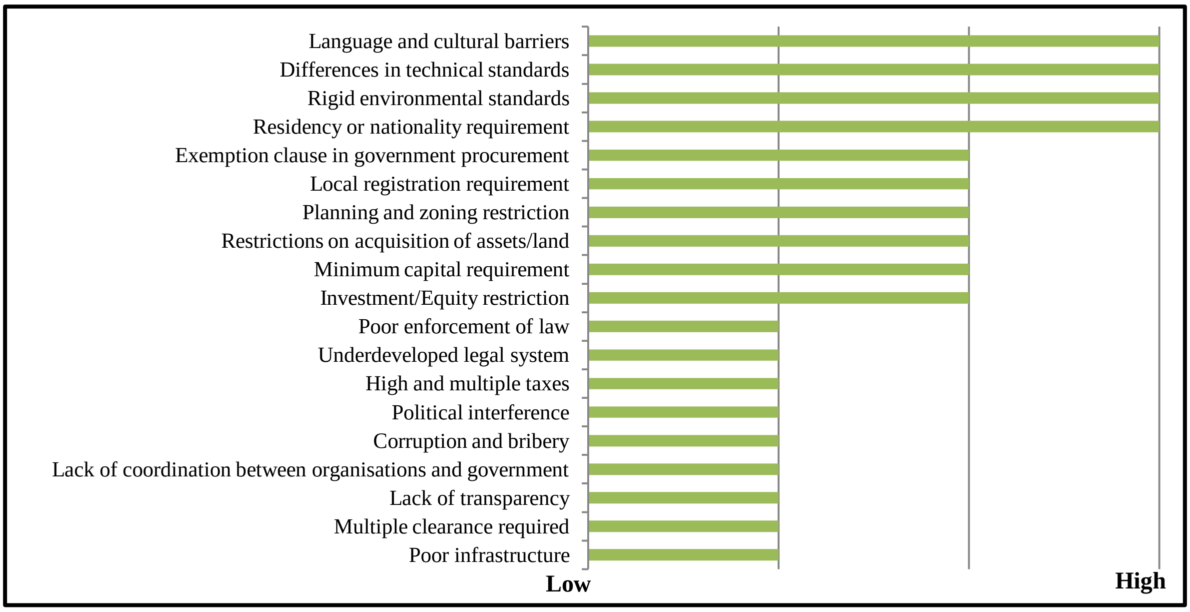
Source: Compiled from DIPP (2013b, 2014).

[38] For details, see *http://www.oecd.org/investment/fdiindex.htm* (last accessed on July 11, 2014).

5.3.2 *Barriers faced by Indian Companies in Germany*

Very few Indian companies gave extreme ranks to the parameters with respect to Germany. Therefore, the ranks were calculated based on 'high', 'normal' and 'low' impact.

Figure 6: Severity of Barriers for Indian Companies



Source: Primary survey.

Factors that have the highest impact are language and cultural barriers, differences in technical standards, rigid environmental standards and the nationality requirement. Barriers that are common in the Indian market such as poor infrastructure, FDI restrictions and corruption hardly exist in the German market.

The participants elaborated on some of these barriers.

- *Language and culture*. Knowledge of German language is a precondition and one has to undergo language training. There are also differences in the work culture between India and Germany. Labour regulations strongly favour the workforce. The labour union regulates the salaries and grading of employees, while the worker council determines work timings.

- *Meeting standards*. Germany has strong health and safety regulations and the standards are much higher than in India. As a result, Indian companies have to make very high investments to meet German standards.

- *Market saturation.* In some sectors the German market is getting saturated and, therefore, there is limited scope for Indian companies to operate and expand. For instance, it is expensive to set up retail banks in Germany; and Indian banks face strong competition from German banks.

- *Local employment*. Most Indian companies have to employ at least 25 per cent German staff, which is not easy to get in terms of skills particularly for software and consultancy services, because most of the good quality workforce is locked up in German companies. Indian companies have to work very hard on employee branding and human resource practices to ensure good quality workforce. The laws related to employing foreign workers are getting tightened and it is likely that in future it would be difficult to employ people on a time and material basis (T&M)[39]. This is a German concept and most information technology service suppliers are employed on this basis. In addition, it is difficult to get an independent professional unless s/he has been appointed to give services for specialised products such as new software.

- *Legal system*. Indian companies consider the stringent legal system in Germany a barrier, as there is no way around the law. This is particularly true for SMEs.

5.3.3 Sector-specific Barriers

The in-depth interviews found useful insights in sectors of interest to Indian and German companies.

- *Information Technology:* Data protection laws in Germany are more stringent than Indian laws and, as a result, companies cannot host any data in India. Indian companies in Germany have to make huge investments in data centres in Germany and the staff has to undergo special training to understand data-specific regulations.

- *Banking:* Unlike other countries where the capital of the parent company is treated as the capital of the branch, this is not the case in Germany. In Germany, each branch has to bring in capital and the total capital from India for that bank is subject to a ceiling of €150 million. In addition, each bank can give a loan of up to 25 per cent of their total capital base. While the EU has strict banking regulations, Germany is more stringent. It follows Basel III[40] norms that encompass more stringent capital adequacy and liquidity requirements than what is already followed in India.

- *Legal Services:* German legal companies need to establish a presence in India to provide information on German laws and regulations and also facilitate business development in both markets. However, foreign lawyers and law firms are not allowed to practise in India.

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[39] Time-and-materials (T&M) contracts may be used to acquire supplies or services. These contracts provide for the payment of labour costs based on fixed hourly billing rates that are specified in the contract. These hourly billing rates include wages, indirect costs, general and administrative expenses and profit. For details, see: http://www.fta.dot.gov/13057_6240.html (last accessed on April 29, 2014).
[40] For details on Basel III norms see http://www.bis.org/bcbs/basel3.htm (last accessed on June 2, 2014)

5.4 Prospects and Expectations

The primary survey found that both India and Germany are potential investment destinations, although the reasons for making investments are different. Since Indian market is growing, Germany has access to wider EU market and both countries are moving towards a regime with unrestricted movement of goods and services, it is likely that opportunities will grow and companies will expand their presence in each other's market.

German companies pointed out that the technology adoption rate has grown in India and Indian companies and the workforce have become accustomed to using new technologies. This has enlarged the scope for investment by German companies in India. Several German companies pointed out that they have plans to set up R&D base in India as the country has a huge advantage in terms of skilled manpower. German companies that invested in R&D in China are keen to shift base from there due to their poor Intellectual Property Rights (IPR) regime and, therefore, by strengthening the regulatory structure, India can become the new R&D base for German companies.

Indian companies pointed out that if German companies invest in technology, India could become a high-quality, low-cost manufacturing destination for German companies. Consequently, Indian companies can upgrade the existing small-scale businesses with new technology.

Both India and Germany have a large number of SMEs and there is scope for enhancing SME collaboration. At present, only a few German SMEs have targeted the Indian market.

While the companies were not well aware of the India-EU BTIA, they suggested that the India-Germany BIPA and DTAA should be revised from time to time to incorporate the changing requirements of corporates in India and Germany. For instance, since the FDI limit in India has been extended in several sectors and foreign companies are buying a greater stake in existing companies, the government should include taxes on dividend under the DTAA. Those who understood the modalities of India-EU BTIA pointed out that trade in services should get similar treatment as trade in goods and the negotiators should aim at achieving a free trade scenario in both goods and services. The government of India should explore the possibility of scheduling commitments under the negative list for the services sector rather than following the General Agreement on Trade in Services (GATS)-type positive list approach. While the EU benefits from free trade in goods, greater benefits would accrue to India under trade in services if the two economies sign the BTIA.

Most companies were also in favour of removing restrictions on movement of people under the India-EU BTIA since it would facilitate business development. Several companies pointed out that the BTIA might help reduce paper work and streamline procedures. The negotiations should go beyond the normal negotiating points and aim at having simplified procedures for EU companies in India and vice versa.

India is a high tariff country. Since India has given different tariff concessions to different trading partners, on the one hand, FTA utilisation is low and tariff lines are complex and on the other hand, there are cases of tariff hopping and inverted duties. India should examine its tariff structure and simplify tariffs. Unilateral tariff reduction will enhance India's bargaining power in trade negotiations. Sometimes, domestic non-competitive industries are protected by high tariffs. They should be helped to improve their technology and skills rather than protected through high tariffs. Respondents said that India should re-examine its incentive schemes. Incentives should be targeted at high-value manufacturing, better technology, environment-friendly and clean energy processes and SMEs. Incentives should be designed so that they are not actionable under the WTO.

The survey participants identified certain sectors for collaboration between India and Germany. India and Germany can have institutional collaboration for product development, language training and cultural exchange. The two countries can collaborate in sectors such as biomedicine, pharmaceuticals and engineering. Moreover, they can foster knowledge sharing and create awareness about each other's market. In addition, there is a need to generate greater awareness about the India-EU BTIA by engaging businesses in the negotiations from time to time and by publishing timely and transparent information about the progress of negotiations for the agreement to be encompassing.

6. Addressing Barriers through Reforms and Negotiations

The overall discussion show that India and Germany have a close diplomatic and economic relationship; and trade and investment flows between the two countries have increased over time. The two countries are trying to strengthen their relationship further through bilateral inter-governmental dialogues and agreements (such as the BIPA) and through a comprehensive trade agreement known as the India-EU BTIA. As a member of the EU, Germany has a keen interest in the successful conclusion of the BTIA. Once signed, the BTIA will be the EU's first comprehensive trade agreement with a large emerging market. If barriers to trade and investment are removed or even reduced under the BTIA, it is likely to benefit both German and Indian companies in each other's market. German companies can have better access to the large and unsaturated Indian market; they can diversify their risks and establish production networks in Asia. At present, a large proportion of the German investment in Asia is in countries such as China but there is scope for German companies to invest in India, especially in manufacturing, given that the Indian government has come up with several policies that favour manufacturing, including the establishment of economic corridors, the National Manufacturing Policy and the SEZ policy. India needs investment in infrastructure and investment by German companies in sectors such as green energy, construction and logistics will be beneficial for India.

India's outward investment in Germany has shown an increase and Indian companies are investing in Germany to acquire technology and access the wider EU market. A comprehensive trade agreement with the EU would not only give Indian companies preferential access to the EU market, but also help to reduce some of the investment barriers. Companies from the two countries can leverage their mutual strengths and collaborate in third-country markets. Despite these benefits the progress of the India-EU BTIA negotiations is slow, Indian and German companies face several barriers in each other's market and reforms in both countries have slowed down, partly due to the global slowdown and other macro-economic and political instabilities.

India and Germany have strong trade and investment complementarities. Germany is one of the largest investors in India and India's investment interest in Germany is also rising. Germany is a key investor and supplier of technology products in the world and in India. Over time, the technology adoption rate in India has increased and Indians companies are acquiring foreign companies for technology transfer. This has led to an increase in Indian investment in Germany. In addition, recently several German companies have started pulling out their investments from China due to the weak regulatory regime and low property rights protection. This places India in an advantageous position and opens a new outlet for German companies interested in emerging markets and, therefore, there is both scope and potential for enhancing bilateral investments between the two countries.

At the institutional level, India and Germany have undertaken several steps to promote bilateral investments. However, bilateral investment flows are still below potential due to the barriers faced by Indian and German companies in each other's market. On this, German companies referred to the multilayered bureaucracy that results in multiple regulations, corruption and bribes, poor regulatory and legal enforcement, infrastructure bottlenecks, issues related to taxation and profit repatriation. Indian companies considered market saturation, language and cultural differences, difference in standards (which are often higher than the EU standards), local employment requirements and rigid labour laws as some of the key barriers. The nature of the barriers shows that there is a need for unilateral domestic reforms in India and both countries should work together to address some of these barriers.

6.1 What India Should Do

India has developed itself as an attractive destination for foreign investments. However, in many sectors such as infrastructure and manufacturing, investment flows are still below the country's potential. There are several barriers to investment. The barriers faced by German companies in India are also faced by other foreign investors and, therefore, if these barriers are addressed India is likely to receive the desired foreign investment. First, the Indian government should streamline the approval process and reduce delays in approval. Here, India can learn from how Germany has streamlined the administrative processes through the use of technology. The use of technology and on-line clearances will reduce the scope for bribe and corruption, which is a major barrier faced by German companies in India.

Second, India should progressively reduce the FDI barriers in sectors such as retail and insurance. It is important to note that in sectors such as retail, FDI restriction is not an entry barrier since a foreign retailer can operate in India through other routes, such as wholesale cash & carry and franchising. However, it limits their ability to select the best route of entry, while the Indian government is losing much-desired FDI. Unless foreign companies are allowed to establish end-to-end supply chains or production networks, they will not be keen to invest in India.

Third, India should strengthen its IPR regime, and outdated regulations that affect international businesses should be replaced by new regulations to facilitate investment. For example, the Right to Fair Compensation and Transparency in Land Acquisition, Rehabilitation and Resettlement Act, 2013 is pending in Parliament. Unless there is a clear policy on land acquisition, business will not be keen to invest.

Fourth, although taxes are high in India, German companies have not raised them as an issue since taxes are also high in Germany. However, they have raised concerns about the changes in the tax policy, which are often sudden and are not supported by stakeholders' consultation (as has been the case in the withdrawal of the Minimum Alternative Tax –MAT exemption) and they have concerns related to transfer pricing. The delay in implementation of the single goods and services tax (GST) is preventing companies from establishing a pan-India supply chain. GST should be implemented at the earliest. Once the GST is implemented, India can learn from the German experiences of setting up seamless logistics networks where clearances can be made online at inter-state check posts.

Fifth, the government should work with businesses in a public-private partnership model to develop the supporting infrastructure. This model can be operationalised if the government helps businesses to access basic infrastructure such as land and electricity.

Sixth, reduction of tariffs under a comprehensive FTA is often trade-distorting and hinders the establishment of production networks. Sometimes tariffs are lower for final products and higher for raw materials and intermediate goods. India should unilaterally lower tariffs, which will help to establish production networks.

Seventh, Indian government provides several incentives and subsidies. These subsidies can be actionable under the WTO. The Indian government should review the subsidy and incentive schemes and link subsidies to high-value manufacturing, better technology, green energy, SME promotion, etc. This will enable India to attract more foreign investment.

6.2 What India and Germany Should Do

India and Germany should realise that there is scope for enhancing mutually beneficial collaboration and investments. At present, a large part of the investment by German companies is in China. The labour costs in China are rising and the concentration of investment in one country leads to business risks. German companies have to spread their investments and production networks and the German government policy should support that. The UK is trying to work with the Indian government to encourage investment by UK companies in the Bangalore-Mumbai Industrial Corridor and the Japanese government is working closely with the Indian government to develop the Delhi-Mumbai Industrial Corridor. The German government should also explore opportunities for joint development of industrial clusters, SEZs and National Manufacturing Investment Zones (NMIZs) in states such as Tamil Nadu and Maharashtra where there is a presence of German companies. For example, joint development of automobile and auto-component clusters and the development of infrastructure around the clusters in cities such as Pune can benefit both Indian and German companies.

Second, both India and Germany have a quasi-federal governance structure. Hence, collaboration should not only be at the federal level but also at the state and provincial level. The exchange of information and sharing of market knowledge will help reduce several barriers including barriers related to language and culture.

Third, standards-setting bodies from India and Germany should collaborate and share information. In the long run, the two countries can work together for mutual recognition of standards.

Fourth, India and Germany have entered into several MoUs, but these are not legally binding. A legally binding and strong investment agreement is likely to facilitate investment flows, as it will offer a predictable investment environment. The two governments should focus on SMEs partnership by identifying areas for such partnership. They can also develop industrial clusters in each other's market to facilitate investment. For example, there can be a German cluster in Pune and an Indian cluster in Köln.

Fifth, there is a need to enhance academic and research collaboration between institutions of the two countries in product development and R&D in sectors such as automobile and auto-components, pharmaceuticals, engineering goods and biomedicine. The Indian government is keen on local procurement of electronics hardware, and investment by German companies in this segment in India will benefit them.

Sixth, the governments of India and Germany should push for successful completion of the India-EU BTIA, since this agreement will facilitate trade in goods, services and investment by removing barriers to trade and through trade facilitation measures. In both countries, there is an urgent need to raise awareness among businesses about the benefits of the India-EU BTIA by engaging businesses in the negotiations and sharing information with them in a transparent and timely manner. Some measures that India and Germany can take that may facilitate investment flows are listed in Table 12.

Table 12: Select measures that can be taken by India and Germany to Facilitate Investment Flows

Action	Enacted by	Risk	Advantage
Better organise and disseminate information on web portals.	Both India and Germany through their respective embassies and trade promotion bodies	Differences in individual interpretation of the law	Better flow of information and improved market knowledge of investors
Policy reforms to ensure better operating environment	Indian government	Political instability	Reforms will help India to attract investment. It will provide German companies with regulatory certainty.
Academic collaboration, research and cultural exchanges	Both India and Germany	No risks	Can lead to technology-related investment in both countries and, enhance market knowledge. Improve understanding of each other's organisational structure, work culture, etc.
Strengthening bilateral agreements such as BIPA and DTAA	Both India and Germany	The existing bilateral agreements will cease to exist after the India-EU BTIA is signed	This will ensure operational certainty for investments and help in profit repatriation.
Mutual recognition of standards and qualification	Both India and Germany	The standards of the two countries are widely different and there is lack of information. India has no common accreditation process. Standards in Germany are higher than EU standards	This will ensure sale of products in each other's market and enhance investment flows.
Speed up the India-EU BTIA negotiations	India, Germany and the European Commission	There has been no progress in the India-EU BTIA negotiations. India has now focused on the Regional Comprehensive Economic Partnership (RCEP) negotiations, while the EU is focusing on the Transatlantic Trade and Investment Partnership (TTIP) negotiations with the US.	The India-EU BTIA is the most comprehensive agreement, which will remove barriers to trade and investment and ensure regulatory certainty.

Source: Primary Survey.

6.3 Business-to-Business Collaboration

Business- to-business collaboration between Indian and German companies is taking place either among individual companies or through business associations such as the Indo-German Chamber of Commerce or between business and government. However, the extent of such collaboration is weak. The database of companies kept by the business councils is out-dated. Moreover, any company/ individual can become a member of the Indo-Germany Chamber of Commerce on payment of a specific fee. Joint Chambers should have a list of investors who have investments or are willing to invest in each other's market along with their sector of investment interest. This will help companies identify business partners. They should conduct regular survey-based market research and publish the findings. This will enhance market knowledge among investors from the two countries. It is also important for industry associations and trade bodies to engage in trade negotiations and provide inputs to their respective governments.

Overall, there is significant scope for enhancing bilateral investment flows between India and Germany, which will benefit companies from both countries. If the reforms suggested above are implemented, they will not only enhance bilateral investment flows but also enhance the global competiveness of Indian companies, improve India's ranking in Ease of Doing Business and other indicators, and increase investment inflows in the manufacturing and infrastructure sectors, which Indian needs. Enhanced investment and collaboration between India and Germany will enable companies from the two countries to leverage their mutual strengths and enhance their presence in third-country markets.

7. Conclusion

Bilateral investments between India and Germany have grown overtime and the two countries have the potential to increase it further due to their investment complementarities. India's large, skilled workforce complements the technological capabilities of Germany. German companies are competent in providing infrastructural services and India needs investments in sectors such as construction and logistics. Investments from Germany can help the India to develop manufacturing facilities upgrade technology, develop the organised services sector and reduce unemployment while German companies can improve its global competitiveness and diversify production networks. Germany is the entry route to the EU market and investment in Germany can give access to Indian companies to the EU market.

The paper found that although there is a significant increase in bilateral investments between the two countries, companies from both the countries are facing barriers to investments. The primary survey found that macro-economic and political stability, lack of clarity in regulations (such as the Indian Special Economic Zones Policy), poor law enforcement, lack of incentives and support (subsidies) from Indian government and varied FDI limits across different sectors, among others are some of the key barriers faced by German companies in India. Indian companies also highlighted barriers faced by them in Germany including local employment conditions, nationality requirements and language barrier.

German companies are keen on policy certainty and stable operating environment than piecemeal incentives while Indian companies are eager to collaborate for advance technology. The study suggests that there is a need for a strong legally binding agreement and the two countries need to cooperate for mutual recognition of standards. Domestic reforms and liberalisation of investment regime are key factors for enhancing bilateral investments; and investment agreements are seen as a key tool to achieve this.

The India-Germany BIPA has important provisions, which many bilateral investments agreements (such as Germany-Singapore BIT, etc) do not have. The India-Germany BIPA also accords fair and equitable treatment and full protection and security to investments and investors. The agreement encompasses all provisions for protection of investors and investments in each other's market. However, it does not make any specific liberalisation commitments. Therefore, the India-EU BTIA could be instrumental in binding the sector-wise FDI regime for German companies and also foster greater collaboration between India and Germany. However, since the agreement will over ride the existing bilateral agreements between the two countries, it has to be designed to ensure that the gains from the existing agreements continue to exist. The study suggests that the governments of the two counties should push for early completion of the India-EU BTIA and the BTIA should be approached through a consultative process with the industry in both India and the EU to ensure that the stakeholders are informed and their concerns should be addressed.

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