



INDIA'S WORLD

INTERNATIONAL AFFAIRS • INDIAN INTERESTS

March 3, 2025

INDIA'S CONTROL OF CHINESE INVESTMENT INFLOWS: THE WAY FORWARD

Dhananjay Sahai, Prashant Khurana

Copyright © 2025 by India's World. All Rights Reserved. To request permission to distribute or reprint this article, please visit [Indiasworld.in/privacy-policy](https://indiasworld.in/privacy-policy). Source URL: <https://indiasworld.in/indias-control-of-chinese-investment-inflows-the-way-forward/>



The geopolitical focus these days is on the ‘decoupling’ or ‘de-risking’ between the U.S. and China. India, too, adopted its own set of policies to limit Chinese influence in its economy, based on geopolitical and economic considerations. These policies, however, have evolved as ad-hoc, last minute responses to changing geopolitical/economic circumstances and routinely suffer from a lack of public debate, absence of a structured policy-making process which is needed to take into account views of varied stakeholders, and therefore display critical gaps or nuances. As we show below, India has often appeared reactionary on this front, demonstrating the lack of a structured approach which balances national security with economic growth.

The cornerstone of India’s attempted decoupling with China is Press Note 3/2020 (PN₃) to the foreign direct investment (FDI) policy, published under the aegis of India’s Ministry of Commerce in April 2020. PN₃ restricted direct and indirect FDI from entities based in countries “sharing a land border” with India. Although it didn’t explicitly name China, the timing and focus of the policy made the

target evident. PN₃ mandated government approval for all investments coming from such countries, thereby effectively shutting the door on strategic Chinese investments due to the uncertainty and scrutiny involved in procuring these approvals.

However, it took until August 2023 for the government to move against passive financial investments by China in Indian listed companies. Foreign investors looking to make financial investments through relatively small stakes (less than 10%) in companies listed on Indian stock exchanges are required to obtain registration as a 'foreign portfolio investor' from Securities and Exchange Board of India (SEBI). Beginning in 2023, Foreign Portfolio Investments (FPIs) were required to disclose their ultimate beneficial ownership, making it difficult for entities with any significant Chinese holdings to obtain such registrations. While SEBI did not formally refuse registration to investors with ties to PN₃-impacted jurisdictions, it is known to have significantly slowed down processing of applications from such investors and enhanced scrutiny of their applications.

India's policy isn't unique. It forms part of a global trend aiming for diversified investments and supply chains to hedge against the risk of economic overdependence on China. However, we argue that unlike the U.S. or Europe – which have a defined framework for decision making in such spheres, notwithstanding policy shifts in different administrations – India's approach lacks a transparent legislative or institutional framework and has been driven by ad-hoc considerations of the state of the Sino-Indian relationship on any given day.

Though American systems are not perfect, even the flip flops by Donald Trump and the U.S. Congress on the forced divestiture / ban of TikTok took place after well considered legislation and a contested election. It culminated in developing mechanisms for localising and monitoring data, a model other countries could follow. By contrast, India's blanket ban on TikTok was opaque, enforced by executive fiat, and denied us an opportunity to explore such innovative solutions.

A CONSTRAINING POLICY, IMPOSSIBLE TO ENFORCE

India's restrictions on foreign investments have now had sufficient gestation time, but the following key issues remain unresolved:

1. PN 3 was exceptionally broad in scope, and on a literal reading it requires tracing the full ownership path of every single share of an entity investing in India, up to the very last individual. This is a near-impossible task in complex, nested corporate structures, the actual individual beneficiary could be sitting behind hundreds of entities – even in legitimate transactions.
2. The breadth of PN3 led to banks (tasked with enforcement) arbitrarily applying (without any clear guidance from the government) varying de-minimis thresholds from 5-25%. A de-minimis threshold is particularly relevant for retail investment vehicles and foreign listed companies investing in India, which could in turn have thousands of amorphous small investors/shareholders. It was only by the beginning of 2024 that

a well understood threshold of 10% came to be applied uniformly, though even that is yet to be written down.

3. In many ways, PN3 is impossible to enforce. This is because other jurisdictions are not required to cooperate in information sharing – an investor can use jurisdictions like Mauritius and Singapore, to mask ultimate beneficial owners.
4. Approval criteria remain unclear and arbitrary. There is no exemption or a fast-track approval process for relatively low-risk, high reward sectors such as consumer goods manufacturing, where Indian industry could actually benefit. The lack of transparent standards, guidelines, and thresholds for approving or rejecting investments opens the door to arbitrary decision-making and discourages legitimate investors. For example, approvals often depend on opaque security assessments, which lack clear guidelines or timelines.

Moreover, the economic impact of these Regulations is yet to be fully understood. Data from the Department for Promotion of Industry and Internal Trade (DPIIT) shows a significant decline in Chinese investments, from approximately \$127 million in 2019 to \$3 million in 2024. This is bound to impact the development of sectors like EVs, renewable energy, and battery storage, which China has expertise in. These restrictions have inadvertently cut off India from access to cutting-edge Chinese technology in such select sectors, which have limited strategic/national security considerations. Instead, it coddles domestic companies from competition, reducing the need for them to be efficient and innovate to compete with the best. The absence of exceptional Chinese competitors also hampers transfers of

technologies and learnings to the Indian car market, making domestic players further dependent on trade protectionism.

Current restrictions on Chinese inflows address security concerns but run the risk of hindering innovation, technological advancement and economic growth.

In contrast, U.S. Committee on Foreign Investment in the United States (CFIUS) has provided clear guidelines for evaluating foreign investments, ensuring transparency in decision-making, and involves public and legislative scrutiny from the U.S. Congress. Even in politically contentious cases such as [Nippon Steel's takeover of U.S. Steel](#) where CFIUS has rightfully been [criticised for due process violations, its decision is public](#) and has been appealed. Contrast that with the Indian policy on PN3 approvals where the executive exercises a pocket veto – effectively killing deals by sitting on the approvals without actually providing a reasoned, timely decision which can then be appealed.

AN APPROACH THAT SERVES INDIA'S INTERESTS

India should adopt a more nuanced and comprehensive approach, tailored for closing these gaps. Its policy should be geared towards reducing arbitrariness and balancing the needs and interests of the economy with immediate national security concerns. Some low-hanging fruit to this end are:

1. Limiting the scope of PN₃ restrictions to identified sectors of strategic/national security importance such as defence, telecom, etc. The overarching aim should be to find accommodations – in the form of business restrictions, requirements to have a local partner, etc. – and only in extreme cases where such remedies are not possible, to block deals.
2. The narrower focus of the restriction can then be used to allow time and space to the executive to evaluate deals properly.
3. The PN₃ process should have clearly defined timelines (the current process allows the Ministry of Home Affairs to seek indefinite extensions), with the government being required to record reasons for rejection. Here, an oft quoted concern is that national security matters are sensitive and therefore the analysis cannot always be made public. This is effectively a smokescreen, as judicial precedents in India and abroad have consistently affirmed that principles of natural justice require informing the aggrieved of reasons for denying their rights.
4. Additionally, a mechanism to allow and encourage stakeholder discussions through public consultations and expert committees could be considered. This would allow policy making to include insights from various quarters, and quell public and business concerns, promoting transparency and fairness.
5. Importantly, given the fact that these actions impede freedom of contract and can have wide ranging implications on India's

economic landscape, it is important to require that relevant officials are also subject to periodic review and questioning before parliamentary committees.

Transparent approval processes improve confidence and encourage foreign investment. The narrower focus and enhanced scrutiny of targeted investments will also permit better evaluation of complex corporate structures, reducing the scope for obfuscating ownership patterns. Third Party audits would also assist in locating the ultimate source of funds and the beneficiary of investments.

India's current restrictions on Chinese equity inflows address security concerns but also run the risk of hindering innovation, technological advancement and economic growth. Policy making needs to balance these concerns, adopting a more surgical approach, allowing sector-specific openness and transparency, while maintaining strategic and security considerations. India can look to global peers for best practices to secure its national interest while remaining an attractive investment destination. India must consider the broader global implications for its global trade dynamics. A nuanced approach is key, in an increasingly polarised global order.



Dhananjay Sahai is an Advocate based in New Delhi. He practices before the Supreme Court High Court and various Tribunals in fields including commercial and finance law.

Prashant Khurana is a Mumbai-based attorney. He works with private equity and debt funds and in the domain of technology-enabled services.