Embassy of India
Berlin, Germany

MAKE IN INDIA MITTELSTAND!

Rödl & Partner

NEWSLETTER

FEBRUARY 2024

Investment Support for German Mittelstand Enterprises

IN THIS ISSUE:

Article provided by:

Rödl & Partner

Economic Overview

As February draws to a close, India's economic landscape reflects a blend of promising advancements and notable developments.

Starting with the **latest economic review published by the finance ministry**, India's economy is showing resilience and promising growth potential. Despite facing risks from geopolitical tensions and economic fragmentation, the country is projected to achieve a 7% growth rate in the fiscal year 2025. However, challenges such as disruptions in global trade due to events like the continued attacks in the Red Sea region pose concerns, leading to supply chain disruptions and spikes in commodity prices.

Nevertheless, India's domestic demand outlook appears positive. Household consumption is expected to strengthen, and there are favorable indications for capital formation, driven by improvements in the private capex cycle, enhanced business sentiments, strong balance sheets of banks and corporations, and sustained government focus on capital expenditure.

Furthermore, India retains its position as the fastest-growing major global economy, supported by government policy measures and effective transmission of monetary tightening, which have helped manage inflation within the country. Overall, despite persistent global risks, India's economic fundamentals and proactive policy interventions position it well to navigate uncertainties and sustain its growth momentum.

Thus, India has a significant **opportunity to leverage this momentum** and ascend to become the world's third-largest economy. S&P Global Ratings forecasts India to maintain its status as the fastest-growing country among major economies for the next three years. Nevertheless, S&P also suggests that for India to fully exploit this potential, it should concentrate on improving the qualifications of its workforce and boosting the participation of women in the workforce, which is in line with the government's plans as indicated in the interim budget published this month.

The Interim Union Budget 2024, in a nutshell, underscores a commitment to comprehensive development, aiming for India's transformation into a Developed Nation by 2047. The focus for the next five years will be on empowering youth, women, farmers, and the economically disadvantaged. The 'First Develop India' strategy for the 'Amrit Kaal' period until 2047 prioritizes infrastructure investments, sustaining Foreign Direct Investment (FDI) growth, fostering inclusive development, and promoting key sectors in India. The budget also confirmed the positive positive outlook outlined above, anticipating a decrease in the fiscal deficit from 5.8% to 5.1% and inflation from 6.7% to 5.5% for FY 2024-25, signaling a promising future despite global economic uncertainties.
(For more information on the interim budget, read "An Insight on the Interim Union Budget 2024", page 3-5 in this newsletter.)

Furthermore, the potential free trade agreement between the EU and India remained a prominent topic this month, drawing attention to the evolving relations between the two entities. **According to the Indian Foreign Minister,** there is a positive trajectory in relations with Europe and Germany, with indications of greater cooperation. However, he refrained from committing to a timeline for the long-awaited free trade agreement, citing its complexity. Despite this, there is optimism surrounding the progress in discussions, with a growing understanding of the mutual benefits of collaboration. While hesitant to predict the agreement's signing this year, the Foreign Minister emphasized the overall advancement in relations with Europe across various domains.

Last but not least, this month has also witnessed notable progress in the electric vehicle (EV) industry, signaling positive developments for cleaner mobility in India. A **significant move by the government** to increase the funding for the Faster Adoption and Manufacturing of Electric Vehicles (FAME) India Phase II scheme has been warmly received by industry stakeholders, who see it as a catalyst for improving infrastructure and boosting the adoption of EVs nationwide.

The Ministry of Heavy Industries' decision to raise the funding from Rs 10,000 crore to Rs 11,500 crore underscores the government's commitment to promoting sustainable transportation initiatives. This augmentation of the FAME India Phase II scheme represents a significant step forward in advancing environmental sustainability.

Additionally, **a noteworthy partnership has emerged** between Indian automaker Mahindra & Mahindra and Germany-based Volkswagen Group. Under this agreement, Mahindra & Mahindra will integrate electric components from Volkswagen's MEB platform into its INGLO platform, showcasing collaborative efforts towards innovation and technological progress in the EV sector.

The adoption of Volkswagen's unified cell concept by Mahindra & Mahindra marks a key milestone, establishing Mahindra & Mahindra as the inaugural external partner to utilize this technology. Volkswagen's MEB platform, which is already embraced by multiple renowned brands, underscores the credibility and potential of this collaboration to drive down costs and accelerate the global adoption of electric vehicles.

The MIIM-Team keenly looks forward to the news and developments awaiting us in the coming month.

Maja Yadu, MIIM Project Co-ordinator, Roedl & Partner

An Insight on the Interim Union Budget 2024

The Interim Union Budget 2024 has emphasized on commitment to comprehensive development, envisioning India's transformation into a Developed Nation by 2047. The next five years are poised to witness unparalleled progress, with a particular focus on four pillars: empowering the youth, women, farmers, and the economically disadvantaged.

Further, the 'First Develop India' strategy during the 'Amrit Kaal' (till the year 2047) centers around investments in infrastructure, maintaining growth momentum in Foreign Direct Investment (FDI), fostering sustainable and inclusive development, and promoting the thrust sectors in India.

The Interim Union Budget for 2024 reveals an optimistic outlook, anticipating a reduction in the revised fiscal deficit from 5.8% in the Financial Year (FY) 2023-24 to 5.1% in FY 2024-25. Similarly, inflation is expected to decrease from 6.7% in FY 2023-24 to 5.5% in FY 2024-25. These key economic indicators signal a promising future for the Indian economy, even amidst global economic uncertainties.

The Finance Bill, 2024 presented on 1 February 2024 received Presidential assent on 15 February 2024, and has been enacted.

Given its interim nature, and as was expected the budget did not introduce extensive changes in tax regulations. Some key tax-related amendments/proposals are outlined in the following paragraphs:

Proposals under Direct Tax Regulations

No major amendments in the Direct Tax are introduced, except rationalization of some due dates. Changes enacted are as follows:

- No changes to the income tax rates and slabs in the Interim Union Budget 2024. Accordingly, the income tax rates and slabs for FY 2023-24 to be continued for FY 2024-25.

- Section 206C(1G) of the Income Tax Act, 1961 ('ITA') has been amended to align the same with the Government's Press Release dated 28 June 2023 on scope and rates of Tax Collection at Source ('TCS') for remittances under the Liberalized Remittance Scheme of Reserve Bank of India and remittance towards overseas tour program package. In a nutshell, no new amendments are made and only earlier announcements made via Press Releases and Circulars have now been incorporated into the Income tax law.

- The sunset clauses for startups' deduction, certain categories of income of International Financial Services Centre ('IFSC') units are extended from 31 March 2024 to 31 March 2025.

- Due Date for Faceless Scheme of Transfer Pricing Officer, Dispute Resolution Panel, Appellate Tribunal has been extended from 31 March 2024 to 31 March 2025.

- A significant announcement was made by the Hon'ble Finance Minister to clear out existing outstanding income tax demands in the case of taxpayers up to INR 0.025 Million for the FYs up to FY 2009-10, and INR 0.010 Million for FYs 2010-11 to 2014-15. Such demands are proposed to be written off. The Government expects this move to benefit around 10 Million taxpayers.

- Interestingly, sunset clause for commencement of manufacturing by domestic companies who have opted for lower corporate tax rate of 15 per cent under section 115BAB of the ITA which was 31 March 2024 has not been extended further. It would have to be seen if the full Budget to be announced by the new Government reconsiders this date and extends the last date for commencement of manufacturing for the lower tax rate of 15 per cent to apply. The government has also refrained from making any announcements around Pillar II developments of Base Erosion Profit measures taking place internationally. This could be picked up in the full Budget.

Proposals under Indirect Tax Regulations

- No changes in the rate of tax applicable under the Goods and Services Tax ('GST') and Customs Regulations in the Interim Union Budget 2024. The validity of General Exemptions under the Customs Regulations has been extended from 31 March 2024 to 30 September 2024.

- Input Service Distributor - Registration Compulsory

Vide the Finance Act, 2024 the Government has proposed to amend the definition and applicability of Input Service Distributor ('ISD') along with the manner of distribution of Input Tax Credit ('ITC') via ISD prescribed under Section 2(61) and Section 20 of the Central Goods and Services Tax Act, 2017 ('CGST Act, 2017'). This proposal is in line with the recommendation of the GST Council issued during the 50th GST Council Meeting held on 11 July 2023.

As per the proposed amendment in the Finance Act 2024, a registered person having multiple GST registrations would be mandatorily required to obtain ISD registration to distribute the ITC in respect of tax invoices for common services received by or on behalf of distinct persons i.e. other GST registrations of the registered person.

Further, the common services would include services which are liable to GST under Reverse Charge Mechanism ('RCM). In case of such services, the GST under RCM would be payable by the normal registration in the state of registration of the ISD and the ITC on such GST paid would be distributed by the ISD registration.

It has been mentioned in the proposed Section 20 of the CGST Act, that the manner of distribution of ITC would be prescribed. The current rule i.e., Rule 39 of the CGST Rules, 2017 which provides mechanism for distribution of ITC by an ISD may cease to be valid in light of the above proposal and revised mechanism may be prescribed.

Along with registering as an ISD once the proposed amendment has been notified, the taxpayer having multiple registrations would be required to identify the common services and service providers that need to be redirected to such ISD registration.

- **Penalty for Failure to Register Certain Machines**

This proposal is further to the Notification No. 04/2024 – CT dated 05 January 2024 prescribing a special procedure to be followed by a registered person engaged in manufacturing of pan-masala and other tobacco products where the registered person is required to furnish the details of packing machines used for filling the products mentioned above and packing of packages, in FORM GST SRM-I within the prescribed time.

Vide Finance Act, 2024 it is proposed to impose penalty equal to an amount of INR 0.10 Million for every machine not so registered along with any other penalty prescribed under Chapter XV or any other provisions of this Chapter. In addition to the aforesaid penalty, the machine not so registered could also be liable for seizure and confiscation, unless such penalty is paid, and machine is registered within 3 days of receipt of communication of the order of penalty.

Note: All changes under the GST Regulations would be made effective from a date to be notified.

The continuation of existing policies in the interim budget reflects the government's commitment to consistency and long-term fiscal planning, bolstering industry trust and enhancing the confidence of foreign investors in Indian governance. Further, anticipation also builds where businesses and taxpayers await some major amendments in the final budget to be announced after formation of the new government.

Anand Khetan, Partner, Roedl & Partner
Priyanka Limaye, Associate Partner, Roedl & Partner

Article provided by:

Mittelstand In Focus
Unlocking value through Letter of Credit

Make in India Mittelstand, a pivotal initiative by the Indian government integrates a wide range of support services, which German mid-sized companies can avail for entering the Indian market. Since its launch, collaborative efforts between the Government of India and the Reserve Bank of India (RBI) have resulted in several such initiatives focused on the ease of doing business in India for global entities. In the fifth edition of the Mittelstand in Focus series, we delve into Letter of Credit.

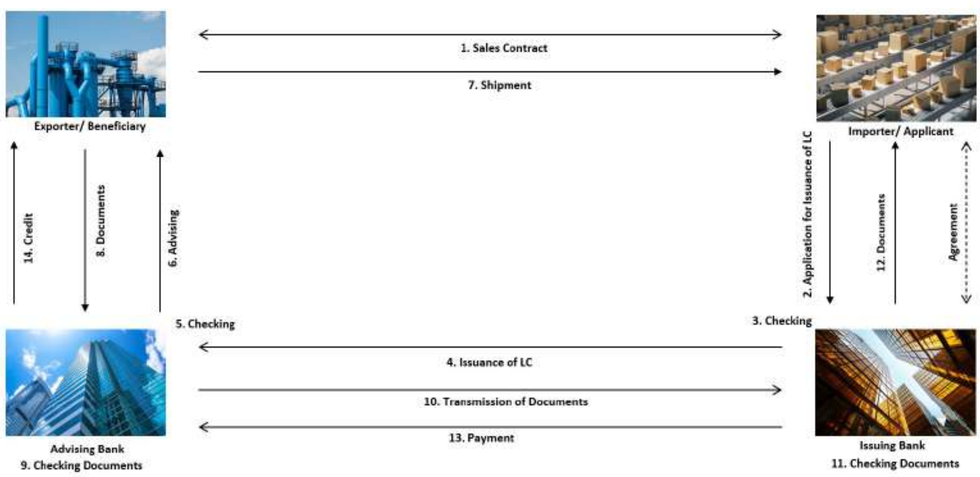
In response to queries received from readers of this periodical, through this article we briefly touch upon the subject of payment methods offered by the Indian Banking industry to facilitate international trade.

Letter of Credit: A Gateway to Secure Trade

At the heart of international commerce, the Letter of Credit (LC) stands as a beacon of financial reliability and trust. This pivotal instrument, also known as a documentary credit, offers an economic guarantee from Deutsche Bank, ensuring that exporters receive timely and accurate payments for their goods, contingent upon adherence to the conditions outlined in the LC. It addresses the inherent risks of international trade, bridging the trust gap between parties unfamiliar with each other's legal frameworks.

The LC comes in various forms—Revocable, Irrevocable, Transferable, and Standby—each tailored to meet specific trade needs while providing different levels of security.

Figure 1: the process flow of a LC trade transaction



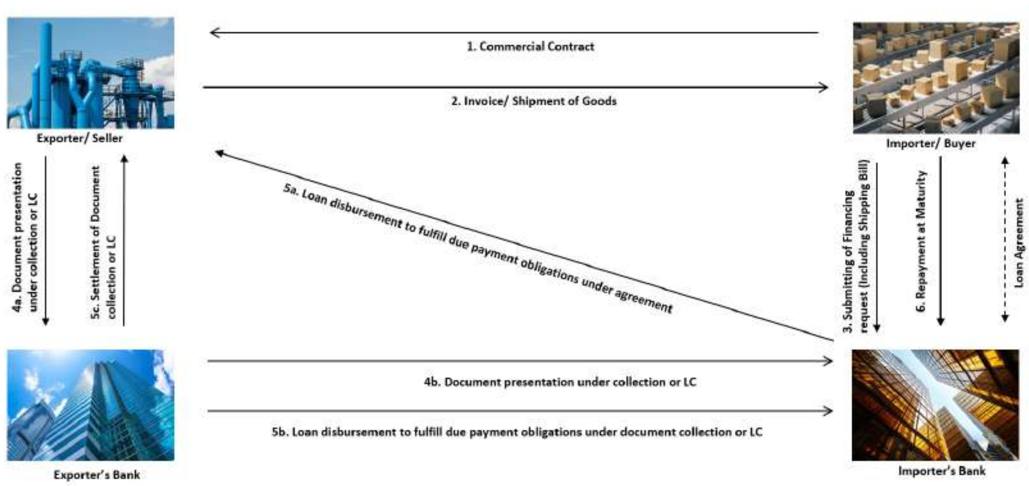
Navigating Legal Frameworks

In India, the essence and operation of LCs are guided by the Indian Contract Act, 1872, and the Sale of Goods Act, 1930, alongside the international standards set by the Uniform Customs and Practice for Documentary Credits (UCP 600) from the International Chamber of Commerce. The RBI further strengthens this framework with guidelines that streamline the opening and operation of LCs by Indian banks, ensuring a smooth and compliant trade process.

Enhancing Liquidity through LC Discounting

LC Discounting emerges as a strategic solution for businesses seeking to accelerate their cash flow. By allowing the beneficiary to receive the present value of the LC amount before maturity, this process not only provides immediate working capital but also mitigates the waiting period associated with payment terms. It is especially beneficial in the context of export LCs, offering a lifeline for businesses in need of urgent liquidity.

Figure 2: the process flow of LC Discounting



Capex LC: Unleashing Capital Efficiency

For enterprises engaged in large-scale capital projects, Capex LC Discounting is a game-changer. It liberates cash flow tied up in credit periods, enabling businesses to sustain operations and continue their investment activities without the burden of liquidity constraints, thereby fuelling growth and innovation.

Deutsche Bank's support to clients

Deutsche Bank stands at the forefront of supporting clients by facilitating smooth transactions involving the complex LC landscape. Our leadership in offering comprehensive LC solutions is a testament to our unwavering dedication to client success. With state-of-the-art platforms for automating import and export flows and a specialized Foreign Exchange Management Act (FEMA) desk for regulatory compliance, we empower our clients with efficient liquidity management and risk mitigation strategies. Our commitment to delivering enhanced yields and managing foreign currency exposures underscores our role as a steadfast ally to our clients in their international trade endeavours.

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Foreign Investment Regulations to Fuel India's Growth Story

Policies focusing on improving the ease of doing business and continued reforms have been a major enabler for drawing foreign investments in the country. With India continuing to remain an attractive destination for global players looking to invest, the Government is expected to continue in the same spirit, implementing key measures to invite global investors to participate in the India growth story.

According to the Department for Promotion of Industry and Internal Trade (DPIIT), FDI in India declined 22% to USD 48.98 billion in the period January to September 2023, due to the global recession. The inflow was at USD 62.66 billion in the year-ago period. However, India is broadly in line with the overall trends of FDI growth. With the view of ease of doing business, better structural reforms in both financial and securities market in India can be expected.

Changes in the regulatory framework

Considering the year of general elections, the Government is expected to continue a slew of reforms to ease foreign investment in India. Currently, cross-border transactions that permit overseas companies with underlying Indian investors to invest back into India, so long as the overseas structure is within two levels of subsidiaries is permitted. However, such cross-border transaction is expected to be further liberalised to attract foreign investments into India.

Press Note 3 clarifications

There is an expectation of clarifications being issued with respect to Press Note 3 (2020 Series). This is to ease issues being faced by institutional investors having minimal exposure to neighboring countries, particularly for transactions involving industries that the Government wishes to promote, and which brings in new technological advancement. These restrictions were placed in 2020 towards the initial stages of the pandemic to protect the Indian economy and avoid opportunistic takeovers and acquisitions. A fast-track process for an expedited security clearance and approval mechanism to process the pending or prospective FDI proposals may also be established.

Sectoral reforms

The Government is expected to further liberalise sectors for FDI, increase existing FDI limits and relax sectoral conditionalities to diversify investing focus in India, and facilitate ease of doing business. Sectors such as pharma, food processing and medical appliances could see a jump in FDI due to the PLI scheme in place.

As the financial landscape continues to evolve, the Reserve Bank of India's (RBI) proactive approach ensures that the financial services sector remains well-updated. Accordingly, the RBI introduced a new scale-based approach for classifying non-banking financial companies (NBFC) and has consolidated the laws applicable to non-systematically important and systematically important NBFCs. Further liberalisation of NBFCs investing in financial services activities abroad can also be expected especially those spaces that facilitate new age fintech services.

This article is part of a consolidated document ("Foresight 2024"). Foresight 2024 is Khaitan & Co's flagship publication that gazes into the proverbial crystal ball and discusses the key themes and stories that will play out over the course of 2024 in India.

Moin Ladha, Partner, Khaitan & Co

Upcoming Events

7TH MIIM EXCHANGE PLATFORM

Berlin | 19.03.2024

Register here for the event.

Stay tuned for many more events!

About MIIM

MIIM is a market-entry support programme for German Mittelstand and family-owned enterprises launched by Embassy of India Berlin, Germany in 2015; driven by Government of India's national programme, 'MAKE IN INDIA'.

The objective of MIIM programme is to facilitate investments by German Mittelstand and family-owned companies in India and to provide market entry related services.

The MIIM program has enrolled more than 196 companies which represent a cumulative declared investment of 1.71 bn EUR to India.

As a part of MIIM program members are exposed to a wide range of business support services under a single platform. The program is being implemented with the support of its Knowledge Partner – Rödl & Partner, Facilitation Partners including Central and State Government Ministries in India and also key industry partners who can support the companies in various aspects of market entry into India. Offered services includes Strategy consulting, M&A, operational market entry support, tax & legal support, financial services and other services

MAKE IN INDIA MITTELSTAND!

Rödl & Partner - Exclusive Knowledge Partner

Investment support for German Mittelstand Enterprises

MIIM Team

MRS. RACHITA BHANDARI
Head MIIM Project Team
Deputy Chief of Mission
Embassy of India, Berlin

MR. SAKETA MUSINIPALLY
Deputy Head - MIIM Project Team
First Secretary
Embassy of India, Berlin

MR. MARTIN WOERLEIN
MIIM Project Team
Head of India Practice
Rödl & Partner

MIIM Hotline:

Email: miim@indianembassy.de | Phone: +49 30-25795514 | Fax: +49-30-25795520

MIIM Team

www.makeinindiamittelstand.de

www.facebook.com/IndiaInGermany

www.twitter.com/eoiberlin

www.linkedin.com/in/miim-make-in-india-mittelstand

Herausgeber/Editors:
Embassy of India

Embassy of India
Tiergartenstraße 17
10785 Berlin
Deutschland/Germany
https://indianembassyberlin.gov.in/
miim@indanembassy.de

Verantwortlich für Inhalt, Layout, Satz / Responsible for content and layout :

Embassy of India
Tiergartenstraße 17
10785 Berlin
Deutschland/Germany
https://indianembassyberlin.gov.in/
miim@indanembassy.de