UAE's exit from FATF grey list to boost FPI flows, investment into Indian NBFCs

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Financial Action Task Force (FATF)

The United Arab Emirates' exit from the the grey list on Friday, nearly two years after its inclusion by the Financial Action Task Force, will ease the road for the country's investors seeking to acquire significant influence in Indian NBFCs.

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An RBI circular in 2021, had stated that investments in NBFCs from FATF non-compliant jurisdictions would not be treated at par with that from compliant jurisdictions.

New investors from or through non-compliant FATF jurisdictions, whether in existing NBFCs or in companies seeking Certification of Registration, were barred from acquiring 'significant influence' in the investee company, either directly or indirectly. Fresh investors were disallowed from having voting power exceeding the 20 per cent threshold.

"India has seen an increase in investment from the UAE in the recent past, including private equity and sovereign wealth funds. The country's removal from the grey list will only help bolster such investment, especially into regulated sectors such as NBFCs," said Parul Jain, Head of Fund Formation Practice at Nishith Desai Associates.

In 2020, the RBI had rejected several applications for greenfield investments or acquisitions in NBFCs routed through private equity and venture capital funds (PE/VC) domiciled in Mauritius after the latter was put on the FATF's grey list.

"The restrictions imposed on UAE investors looking to invest in India-based PE/VC funds and the financial services sector are now eased. Similarly, India-based PE/VC funds that want to invest in portfolio companies located in the UAE can now do so with fewer obstacles. This could potentially lead to an increase in cross-border investments and collaborations between the two countries," said Yashesh Ashar, Partner, Illume Advisory.

The exit may ease KYC requirements for FPIs from the region, boost inflows and catapult UAE to the list of top 10 regions for FPI flows into India over the next two years, according to experts.

"Post the UAE-India agreement, trade between the two jurisdictions have increased. Friday's announcement has the potential of doubling the number of FPI registrations and bringing in larger ticket size inflows," said Viraj Kulkarni, Founder, Pivot Management Consulting.

The UAE had 143 FPIs registered in India two years ago. That number has swelled to 198, the majority of which are Category II investors, NSDL data showed.

Kulkarni believes that the exit will reduce the cost of funding for UAE-based banks and reduce their dependence on wealthy clients from the region. As cost reduces and the fund flow from other countries improves, some of it will find its way to India as FDI or portfolio flows.

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The exit could enhance or reinstate UAE's reputation as a fund jurisdiction, potentially creating competition for the GIFT IFSC, said Ashar.

India and the UAE recently signed eight pacts, including a bilateral investment treaty and a framework deal to foster regional connectivity.

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