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Dr. Manoranjan Sharma
(Chief Economist)

THE 'INVESTMENT FRIENDLINESS INDEX OF STATES' - ISSUES AND CONCERNS

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The 'Investment Friendliness Index of States' (IFI) is a composite ranking that evaluates how well a state fosters business growth, investment inflows, and economic development.

Conceptual and Methodological Framework

The index typically includes parameters such as Ease of Doing Business (regulatory framework, business registration time, transparency); Infrastructure (transport, energy availability, industrial parks); Economic Stability (GDP growth, per capita income, inflation rate); Taxation and Incentives (corporate tax rates, subsidies, special economic zones); Labor Market and Workforce (availability of skilled labor, wage rates); Innovation and Technology Ecosystem (R&D investments, tech hubs, startup support); Legal and Policy Environment (contract enforcement, corruption levels, investment protection); Cost of Living and Quality of Life (housing costs, healthcare, lifestyle attractiveness); Sustainability and ESG Compliance (environmental regulations, green investments); and FDI and Business Sentiment (foreign direct investment inflows, investor perception).

IFI was launched in 2025 to promote the spirit of competitive cooperative federalism by identifying constraints to investment, promoting healthy competition among states to attract private investment, and fostering accelerated economic growth and structural transformation across states. The index will rank states around two primary dimensions of opportunity and risk. Both these dimensions will have at least four sub-indicators to rank the performance of states.

The sub-indicators under the opportunity dimension, which will have a weightage of 65%, will include the state government's policy and incentives, infrastructure, business climate, innovation, and available resources in the states.

The risk dimension will have a weightage of 35% and will include pillars like natural risk, regulatory risk, financial risk, and institutional effectiveness.

Further, in all four sub-categories of opportunities and risks, a few perception-based indicators will also be included to measure how investors perceive and prioritize opportunities and risks, or to assess the quality of investor experience on certain rules and regulations.

Implementation of the Index

This Index on investment efficacy, focusing on opportunity and risk dimensions, is also likely to address regulatory hurdles that deter private investment.

India's State Investment Potential Index (N-SIPI) ranks states based on business attractiveness. Top performers include Gujarat (strong infrastructure, top in manufacturing & trade); Maharashtra (Mumbai as financial hub, high FDI inflows); Karnataka (well-developed IT sector, Bengaluru startup ecosystem); Tamil Nadu (strong in automobile & electronics manufacturing); and Telangana (Hyderabad's tech-driven economy, ease of doing business).

While this innovative measure is welcome in enhancing competition among states, thereby improving the overall investment climate in India, gaming the system can lead to an undue reliance on rankings instead of effective and enduring investment.

An index comparing states under various parameters will help these States streamline their regulations to mobilize greater investment, transcending superficial, short-term improvements, and focusing on long-term sustainable development in areas, such as Government policies and tax benefits, industrial clusters and infrastructure, growth potential and market size, and business costs and legal environment.

But there are issues of accentuating regional imbalances stemming from historical and deeply entrenched structural factors, unreliable rankings or rankings not fully representative of the wider ecosystem of a state's investment setting, tweaking financial incentives to boost rankings at the cost of long-term financial stability, rights for labourers, environmental balance, ad-hoc or interim measures to jack up their index rank or repeated policy change hurting es investor confidence by establishing an unpredictable and uncertain economic climate. It, therefore, remains to be seen how this incentive-based initiative for states to improve productivity pans out because the proof of the pudding is in the eating.

Way Forward

The Central Government could make this Index more broad-based and encompassing by including factors like social justice, environmental impact, long-term sustainability, and regional growth. Balanced regional development requires customised initiatives rather than a uniform broad-brush approach oblivious to granular ground-level needs and requirements, credible and transparent data, careful monitoring and evaluation, closer public-private partnerships, and factoring in the interests of all stakeholders to make a perceptible difference.