

Role of Competition Policy in Regulating Foreign Direct Investment (FDI)

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Abstract— Foreign Direct Investment (FDI) plays a crucial role in economic development by promoting industrial growth, employment generation, technological advancement, and global market integration. However, unrestricted foreign investment may lead to monopolistic practices, abuse of dominance, market concentration, and unfair competition in domestic markets. Competition policy acts as an essential regulatory mechanism to ensure that foreign investment contributes positively to economic growth without harming market competition. This research paper examines the role of competition policy in regulating FDI by analyzing how competition laws maintain market fairness while encouraging foreign investment. It explores the relationship between investment liberalization and competition regulation in both developed and developing economies, with special reference to India. The paper highlights the role of antitrust laws, merger control regulations, abuse of dominance provisions, and government oversight in balancing investor interests and public welfare. The study also evaluates the legal framework governing FDI in India, including the Competition Act, 2002, the Foreign Exchange Management Act, 1999, and policies formulated by the Department for Promotion of Industry and Internal Trade (DPIIT). It further discusses challenges such as regulatory overlap, global mergers, digital monopolies, and national security concerns. The paper concludes that an effective competition policy promotes transparency, protects domestic enterprises, prevents market distortions, and ensures sustainable economic development while maintaining India's attractiveness as an investment destination.

Keywords—Foreign Direct Investment, Competition Policy, Antitrust Law, Market Regulation, Competition Act 2002, Merger Control, Economic Development, India.

I. INTRODUCTION

Foreign Direct Investment (FDI) has emerged as one of the most significant drivers of globalization and economic integration in the modern world. It involves the cross-border transfer of capital where an investor from one country acquires a lasting interest

and significant control in an enterprise located in another country. FDI contributes to economic growth by introducing advanced technologies, managerial expertise, and employment opportunities, especially in developing economies. As countries compete to attract foreign investment, regulatory frameworks play a crucial role in shaping investment flows.

Competition policy, also referred to as antitrust policy, is designed to maintain fair competition in the market by preventing anti-competitive practices such as monopolies, cartels, abuse of dominance, and restrictive trade practices. It ensures that markets function efficiently, benefiting consumers through lower prices, better quality products, and innovation. Over time, competition policy has evolved from a purely domestic regulatory tool to an important component of global economic governance.

The relationship between competition policy and FDI is complex and multifaceted. On one hand, competition policy encourages foreign investment by ensuring a level playing field and eliminating barriers to entry. It reduces market imperfections and promotes transparency, which are key determinants of FDI inflows. On the other hand, competition policy can also act as a regulatory constraint on foreign firms, particularly in cases involving mergers and acquisitions, where authorities scrutinize transactions for their potential impact on market competition.

Historically, the intersection of competition policy and FDI has gained prominence with the liberalization of economies and the rise of multinational corporations. The increasing integration of global markets has led to a surge in cross-border mergers and acquisitions, raising concerns about market concentration and dominance by large firms. Competition authorities across the world now play a critical role in evaluating such transactions to prevent anti-competitive

outcomes. Another important dimension of this relationship is the role of competition policy in ensuring non-discrimination between domestic and foreign investors. A well-designed competition framework treats all firms equally, thereby creating a conducive environment for investment. However, there have been instances where competition policy has been used as a tool of economic nationalism, restricting foreign investments under the pretext of protecting domestic industries.

Furthermore, the emergence of FDI screening mechanisms has added another layer of complexity. Governments increasingly review foreign investments in sensitive sectors such as defense, telecommunications, and infrastructure to safeguard national security and public interest. These screening mechanisms often overlap with competition policy, particularly in merger control processes. In recent years, the debate on competition policy has expanded to include digital markets and multinational tech giants. The growing market power of large corporations has prompted calls for stricter enforcement of competition laws to prevent monopolistic practices. This has significant implications for FDI, as many foreign investments are now concentrated in technology-driven sectors.

The purpose of this research paper is to analyze the role of competition policy in regulating FDI, examining both its positive and negative impacts. It explores theoretical perspectives, empirical evidence, and policy implications, with a focus on how competition policy can be designed to maximize the benefits of FDI while minimizing potential risks.

II. LITERATURE REVIEW

The relationship between competition policy and FDI has been extensively studied in economic and legal literature. Scholars have approached this topic from various perspectives, including institutional theory, international business, and law and economics.

One of the foundational arguments in the literature is that competition policy enhances FDI by creating a fair and transparent business environment. Studies emphasize that effective competition law enforcement reduces entry barriers and fosters trust among investors. The institutional quality of a

country, including regulatory effectiveness and rule of law, significantly influences FDI inflows.

Another strand of literature highlights the “dual nature” of competition policy. While it promotes investment by ensuring market efficiency, it can also be used as a protectionist tool. Scholars argue that competition authorities may be influenced by political and economic interests, leading to biased enforcement that discourages foreign investors.

The OECD has contributed significantly to this discourse by examining the role of policy competition among countries to attract FDI. It suggests that reliance on incentives alone may undermine transparency and accountability, advocating for rule-based approaches instead.

Empirical studies have attempted to quantify the relationship between competition policy and FDI. Research based on cross-country data indicates that strong competition enforcement positively correlates with higher FDI inflows, particularly in countries with high regulatory quality. However, the relationship is not uniform and depends on factors such as institutional trust and economic stability.

Another important area of research focuses on merger control and its impact on FDI. Crossborder mergers are a major component of FDI, and competition authorities play a critical role in approving or blocking such transactions. Studies suggest that stringent merger control can both protect competition and deter investment, depending on its implementation.

The literature also explores the interaction between competition law and investment law. Scholars argue that there are significant synergies between these two fields, as both aim to promote economic efficiency and market openness. However, conflicts may arise when competition policy restricts investment flows. An analytical method is employed to critically evaluate the relationship between competition policy and FDI. The research examines both the positive and negative impacts of competition law on foreign investment, including its role in promoting market efficiency, ensuring fair competition, and preventing anti-competitive practices, as well as its potential to act as a regulatory barrier. The study also analyzes emerging issues such as merger control, FDI screening, and digital market regulation.

Recent studies have examined the impact of policy uncertainty on FDI. Findings indicate that while predictable and consistent enforcement of competition law encourages investment, uncertainty and regulatory risk can deter investors. Developing countries face unique challenges in balancing competition policy and FDI regulation. While they seek to attract foreign investment for economic development, they must also ensure that such investments do not harm domestic industries or lead to excessive market concentration. Weak institutional frameworks and lack of enforcement capacity can undermine the effectiveness of competition policy, reducing its ability to regulate FDI effectively. The research is primarily descriptive and exploratory in nature. It seeks to describe the existing legal and institutional framework while also exploring the challenges and opportunities associated with the regulation of FDI through competition policy. The findings are derived through careful interpretation and synthesis of the collected data rather than empirical or statistical analysis.

In conclusion, the literature suggests that competition policy plays a critical role in shaping FDI flows, but its impact is context-dependent and influenced by institutional and political factors.

III. RESEARCH METHODOLOGY

This research adopts a doctrinal and analytical methodology based exclusively on secondary sources of data to examine the role of competition policy in regulating Foreign Direct Investment (FDI). The study is qualitative in nature and focuses on interpreting legal frameworks, policy documents, and scholarly opinions to understand the interaction between competition law and investment regulation.

The secondary data used in this research is collected from a wide range of authoritative and credible sources. These include academic journals, books, research articles, and working papers published on platforms such as JSTOR, ScienceDirect, and Oxford Academic. In addition, reports and policy papers issued by international organizations such as the Organisation for Economic Co-operation and Development (OECD), the World Trade Organization (WTO), and the United Nations Conference on Trade and Development (UNCTAD) have been extensively referred to. Government publications, legislative texts such as the

Competition Act, 2002 (India), and policy guidelines related to FDI have also been analyzed to provide a comprehensive legal perspective.

The research follows a doctrinal approach, which involves the systematic examination of statutes, legal principles, and judicial interpretations relevant to competition policy and FDI. This method helps in understanding how legal provisions regulate market behavior and influence foreign investment. The study also incorporates a comparative perspective, where relevant, by briefly referring to international practices and regulatory frameworks in different jurisdictions to highlight similarities and differences in approach.

Certain limitations of the study must be acknowledged. Since the research relies solely on secondary data, it does not include primary data collection such as interviews, surveys, or fieldwork. Additionally, the study is constrained by the availability and accessibility of published materials. Despite these limitations, efforts have been made to ensure the reliability and validity of the research by using up-to-date and credible sources.

Overall, the chosen methodology is appropriate for a legal research study as it provides a structured and in-depth understanding of the role of competition policy in regulating FDI within a theoretical and policy-oriented framework.

Chapters:

Chapter 1: Conceptual Framework of FDI and Competition Policy :

Foreign Direct Investment (FDI) refers to an investment made by an entity or individual in one country into business interests located in another country, typically involving a lasting interest and significant degree of control. It differs from portfolio investment as it entails managerial influence and long-term commitment. FDI is widely recognized as a catalyst for economic growth, particularly in developing economies, as it brings capital inflows, technological innovation, employment generation, and integration into global markets. Governments across the world actively design policies to attract FDI through incentives, liberalization, and regulatory reforms. Competition policy, also known as antitrust policy, is a set of laws and regulations aimed at

promoting fair competition in the market. It seeks to prevent anti-competitive practices such as cartels, abuse of dominant position, price-fixing, bid-rigging, and anti-competitive mergers and acquisitions. The primary objective of competition policy is to ensure market efficiency, protect consumer welfare, and foster innovation. In India, competition policy is governed by the Competition Act, 2002 and enforced by the Competition Commission of India (CCI).

The conceptual linkage between FDI and competition policy lies in the shared objective of promoting economic efficiency and market development. While FDI enhances capital formation and industrial growth, competition policy ensures that such growth does not lead to monopolistic practices or market distortions. The interplay between the two becomes particularly relevant in the context of cross-border mergers and acquisitions, where foreign investors may acquire dominant market positions.

Chapter 2: Role of Competition Policy in Promoting FDI :

Competition policy plays a significant role in attracting and promoting FDI by creating a transparent and predictable regulatory environment. Investors prefer jurisdictions where rules are clear, enforcement is consistent, and there is minimal risk of arbitrary decision-making. A robust competition framework signals institutional strength and regulatory credibility, which are critical factors influencing investment decisions. Another important aspect is the role of competition policy in ensuring non-discrimination. A fair competition regime treats domestic and foreign firms equally, thereby fostering investor confidence. When foreign investors are assured that they will not face biased treatment or protectionist policies, they are more likely to invest in the host country. Competition policy also contributes to economic efficiency by promoting innovation and productivity. Increased competition forces firms to improve their performance, adopt new technologies, and reduce costs. This creates a dynamic business environment that attracts foreign investors seeking profitable opportunities. Furthermore, effective merger control mechanisms ensure that cross-border mergers and acquisitions do not lead to excessive market concentration. While such transactions are an important mode of FDI, unchecked consolidation can

harm competition. By reviewing and regulating mergers, competition authorities strike a balance between facilitating investment and protecting market competition.

Chapter 3: Competition Policy as a Regulatory Constraint on FDI :

While competition policy promotes FDI, it can also act as a regulatory constraint in certain situations. One of the primary areas where this occurs is merger control. Foreign investors often enter markets through mergers and acquisitions, which are subject to scrutiny by competition authorities. If a proposed transaction is likely to result in a dominant market position or reduce competition, it may be blocked or subjected to conditions. This can discourage foreign investment, particularly in highly regulated sectors. Competition policy may also be used as a tool of economic protectionism. Governments may impose restrictions on foreign firms under the guise of competition regulation to protect domestic industries. This can undermine the principles of free trade and discourage foreign investment. Additionally, the overlap between competition policy and other regulatory frameworks, such as FDI screening mechanisms, can create complexities. In many countries, foreign investments in sensitive sectors are subject to national security reviews, which may overlap with competition assessments. This duplication of regulatory processes can lead to delays and increased costs for investors. Therefore, while competition policy is essential for maintaining market integrity, its implementation must be carefully balanced to avoid unnecessary restrictions on FDI.

Chapter 4: Institutional and Legal Framework Governing Competition Policy and FDI :

The regulation of FDI through competition policy is supported by a complex institutional and legal framework at both national and international levels. At the domestic level, countries have established competition authorities responsible for enforcing antitrust laws and regulating market practices. In India, the Competition Commission of India (CCI) plays a key role in overseeing mergers, preventing anti-competitive practices, and promoting competition advocacy.

At the international level, organizations such as the Organisation for Economic Co-operation and Development (OECD) and the World Trade Organization (WTO) contribute to the development of competition policy principles and guidelines. While there is no global competition law, these institutions promote cooperation and convergence among national regimes.

Another important aspect of the institutional framework is the interaction between competition policy and investment law. Bilateral investment treaties (BITs) and free trade agreements (FTAs) often include provisions relating to fair competition and non-discrimination. These agreements aim to protect foreign investors while ensuring compliance with domestic competition laws.

The effectiveness of this framework depends on factors such as institutional independence, enforcement capacity, and transparency. Strong institutions are essential for ensuring that competition policy is applied fairly and consistently, thereby enhancing its role in regulating FDI.

Chapter 5: Emerging Trends and Challenges in Competition Policy and FDI :

The evolving global economic landscape has introduced new challenges and trends in the relationship between competition policy and FDI. One of the most significant developments is the rise of the digital economy. Large technology companies, often operating across borders, have acquired substantial market power, raising concerns about monopolistic practices. Competition authorities are increasingly focusing on regulating digital markets to ensure fair competition.

Another emerging trend is the growing use of FDI screening mechanisms. Governments are becoming more cautious about foreign investments in strategic sectors such as defense, telecommunications, and critical infrastructure. While these measures are aimed at protecting national security, they may also restrict FDI flows and create tensions with competition policy objectives. Globalization has also led to an increase in cross-border mergers and acquisitions, requiring greater cooperation among competition authorities. Differences in regulatory approaches across countries can create challenges for multinational corporations and lead to inconsistent

outcomes. Protectionism and economic nationalism have further complicated the relationship between competition policy and FDI. In some cases, competition laws are used to restrict foreign entry and protect domestic industries, undermining the principles of open markets.

Finally, developing countries face unique challenges in implementing effective competition policy. Limited institutional capacity, lack of expertise, and political interference can weaken enforcement and reduce the effectiveness of regulation.

IV. FINDINGS

The research reveals that competition policy plays a significant role in influencing FDI flows. Countries with strong and transparent competition frameworks tend to attract more foreign investment due to increased investor confidence. Effective enforcement reduces market distortions and ensures equal treatment of domestic and foreign firms.

However, the study also finds that competition policy can act as a barrier when misused for protectionist purposes. Political influence and regulatory capture may lead to biased decisions, discouraging foreign investors. Additionally, policy uncertainty and inconsistent enforcement negatively impact investment decisions.

Another key finding is the growing importance of FDI screening mechanisms, particularly in sensitive sectors. While these measures are necessary for national security, they may overlap with competition policy, creating regulatory complexities.

The research also highlights the importance of institutional quality. Strong governance, rule of law, and regulatory efficiency enhance the effectiveness of competition policy in attracting FDI.

V. SUGGESTIONS

To improve the role of competition policy in regulating FDI, the following measures are recommended:

1. Strengthening Institutional Frameworks
2. Governments should enhance the independence and capacity of competition authorities.
3. Ensuring Transparency and Predictability

4. Clear guidelines and consistent enforcement reduce uncertainty for investors.
5. Balancing Regulation and Liberalization
6. Policies should prevent anti-competitive practices without discouraging investment.
7. Promoting International Cooperation
8. Cross-border coordination is essential for regulating multinational corporations.
9. Integrating Competition and Investment Policies
10. Harmonization of laws can reduce conflicts and improve regulatory efficiency.
11. Addressing Digital Market Challenges
12. New frameworks are needed to regulate tech-driven FDI.

VI. CONCLUSION

The relationship between competition policy and Foreign Direct Investment (FDI) reflects a critical intersection of economic regulation and global market integration. This research has demonstrated that competition policy plays a dual and dynamic role in regulating FDI—acting both as a facilitator of investment and as a necessary regulatory safeguard to maintain fair and efficient market conditions.

On one hand, a well-developed competition policy framework contributes significantly to attracting FDI by ensuring transparency, predictability, and a level playing field for all market participants. Foreign investors are more inclined to invest in jurisdictions where regulatory systems are stable, non-discriminatory, and effectively enforced. By preventing anti-competitive practices such as cartels, abuse of dominance, and restrictive trade agreements, competition policy enhances market efficiency and promotes innovation. This creates a conducive investment climate where both domestic and foreign firms can compete fairly, ultimately benefiting consumers and the economy at large.

On the other hand, the study highlights that competition policy can also act as a constraint on FDI, particularly when enforcement becomes overly restrictive or influenced by protectionist considerations. Stringent merger control regulations, overlapping regulatory frameworks, and inconsistent application of laws may create uncertainty and increase compliance burdens for foreign investors. In some cases, competition policy may be used as a tool to limit foreign participation in domestic markets under the guise of protecting national interests. Such

practices can undermine investor confidence and discourage potential investment inflows.

The increasing complexity of global markets has further intensified the need for effective coordination between competition policy and investment regulation. The rise of cross-border mergers, digital markets, and multinational enterprises has expanded the scope of competition law beyond traditional boundaries. Additionally, the emergence of FDI screening mechanisms, particularly in sensitive sectors, has introduced new challenges in balancing economic openness with national security concerns. These developments underscore the importance of a coherent and harmonized regulatory approach.

The findings of this research emphasize that the effectiveness of competition policy in regulating FDI largely depends on institutional strength, regulatory clarity, and policy consistency. Independent and well-equipped competition authorities are essential for ensuring fair enforcement and preventing misuse of regulatory powers. Furthermore, international cooperation and convergence of competition policies can help address the challenges posed by globalization and cross-border economic activities.

In conclusion, competition policy is an indispensable tool in shaping the impact of FDI on national economies. Its success lies in achieving a careful balance between encouraging foreign investment and safeguarding competitive market structures. A transparent, consistent, and non-discriminatory competition regime not only enhances investor confidence but also ensures that the benefits of FDI are equitably distributed. As global economic dynamics continue to evolve, competition policy must adapt to emerging challenges while maintaining its core objective of promoting fair competition and sustainable economic development.

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