A Descriptive Study of Foreign Investment in India

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Abstract

India is representing itself as a vast potential for overseas investment from a very long time. It has been observed during the present BJP led government that constant efforts have been done to encourage foreign investment into the Indian Market. The present paper is an attempt to analyse the prospects and perspectives of foreign direct investment in India. The role of Foreign Direct Investment has been discussed. Also, the trends of foreign investment in India are observed for the purpose. The findings reveal that the benefits of foreign direct investment outweigh the cost of foreign investment in India. In addition, the study concluded that the flow of investment in India is contributing towards the growth of Indian economy. Also, the findings show that in spite of various economic reforms to encourage foreign investment in India, India is not able to attract foreign investment at a fast pace and it has hit a five year low.

Introduction

Foreign investment means investment made in a country by a resident of a foreign country. The resident may be an individual, corporate enterprise or any institution. Foreign investment takes the two forms especially: Foreign Direct Investment (FDI) and Foreign Portfolio Investment (FPI).

Foreign Direct Investment

FDI is a good source of capital, technical and managerial know-how. FDI are the net inflows of investment to acquire a lasting management interest (10 percent or more of voting stock) in an enterprise operating in an economy other than that of the retail investor. It is an investment made by foreign resident entity in an enterprise resident of the host country so as to build a long term relationship with the host country. The main aim of FDI is to take participation in the management and control of host country firms, and to help in increasing the production activities. FDI is possible through various means like Joint ventures, mergers and acquisitions, technical collaborations, strategic alliances or any other popular means. It can be called as an instrument of bringing a good governance mechanism in the host country.

Foreign Portfolio Investment

It is not a direct source of investment. Rather, it is an investment made by a foreign investor in the stock market of a foreign country. It includes foreign pension funds, receipts i.e. American Depository Receipts, Global Depository Receipts, mutual funds, asset management companies etc. the main aim of FPI is to make capital available in general for all i.e. through secondary market and not for particular entities. The management and control is not shared by them. The focus is on building short term investments in boom phase of economy and leave the market as there seems to be a signal of trouble. FPI is also called by the name foreign institutional investment (FII).

Objectives of the Study

Since 1951, the Indian financial system has seen a great number of changes in foreign investment policy. The scheme of planned economic development through encouraging transfer of foreign technology was oriented towards building an industrial base in the country. As the time passed by, the focus of the government towards the foreign investment shifted from selective and restrictive policies to liberalise and open door policy. Therefore, the main objective of this study is to get in depth sight over foreign direct investment in India. For the purpose, this paper is focussed upon the following points:

i) To study the prospects of foreign investment in India.

ii) To have knowledge regarding costs and benefits of foreign investment flows.

iii) To compare foreign direct investment and foreign institutional investment flows in Indian economy.

iv) To understand the role and trends of foreign direct investment flows in boosting the growth of the nation.

Review of Literature

This section reviews the literature on Foreign investment in India.

Popli, Gumukh Singh and Kumari (2012) study tried to make a modest attempt of developing an insight as to what are the trends in the Retail Industry of India and to the pros and cons of FDI in this sector. It also focused on whether this policy would be beneficial for the Indian Economy as a whole or not.

Bhattacharyya Jita, Bhattacharyya Mousumi (2012), "Impact of Foreign Direct Investment and Merchandise and Services Trade of the Economic growth in India: an Empirical study" , the study found that there was a long term relationship between FDI, merchandise, service trade and economic growth of India. Bi-directional causality is observed between merchandise trade and economic growth, services trade and economic growth. Unidirectional causality is seen from FDI to economic growth and FDI to merchandise trade. A unidirectional causality is also observed from merchandise trade to services trade.

Shalini,Ankush and Ritu (2012) paper tried to study the need of FDI in India, to exhibit the sector-wise & year-wise analysis of FDI's in India, to rank the sectors based upon highest FDI inflows. The results show that Mauritius is the country that has invested highly in India followed by Singapore, Japan, and USA and so on. It also shows that there has been a tremendous increase in FDI inflow in India during the year 2000 to 2011.

Saini A., Law S. H., Ahmad A. H. (2010), "FDI and economic growth: New evidence on the role of financial markets", the study proved that the positive impact of FDI on growth "kicks in" only after financial market development exceeded a threshold level. Until then, the benefit of FDI was not in existence.

Singh J. (2010), "Economic Reforms and Foreign Direct Investment in India: Policy, Trends and Patterns", study tried to analyze the emerging trends and patterns of FDI inflows into India in response to various policy measures announced by the Government of India since mid-1980 and later. The empirical analysis suggested that the FDI inflows, in general, show an increasing trend during the post-reform period. Furthermore, country-wise comparison of FDI inflow also indicated that FDI inflow into India had increased considerably in comparison to other developing economies in the recent years. Thus, the study indicates that the FDI inflows into India responded positively to the liberalization measures introduced in the early 1990s.

Singh, Shikha (2009), "Foreign Direct Investment (FDI) and Growth of States of India"

This study stated that foreign direct investment (FDI) policies and economic growth of developing countries around the world. Attracting FDI inflows with conducive policies had therefore become a key battleground in the emerging markets.The prospect of new growth opportunities and outsized profits encouraged large capital inflows across a range of industry and opportunity types. And this had led to competition among the states in formulating flexible policies and providing incentives to woo private investors to invest more and more. In the light of the above the paper highlighted the trend of FDI in India after the economic reforms, sector-wise and country-wise share of FDI, the manner in which FDI has effected the growth of Indian states. Various factors which played a significant role in attracting FDI into a particular state are also examined. Efforts made by the state governments in order to attract maximum FDI were also studied.

Keshava, Dr. S.R. Rathnamma (2008), The Effect of FDI on India & Chinese Economy: A Comparative Analysis: stated that India and China are the two emerging economic giants of the developing world, both situated in Asia with 37% of world population (Asian Development Outlook2005) and with more than 9% growth in their respective GDP of their economies (World Development Report 2006). China got independence in 1949, after 2 years of India's political Independence (1947), but today China has surged far ahead of India in socio-economic development indicators. The FDI in India is just 3.4% of FDI flows as a percentage of Gross Fixed Capital Formation in India by 2004 and 5.9% of FDI stocks as a percentage of GDP by 2004, whereas in China it was 8.2% of FDI flows as a percentage of Gross Fixed Capital Formation and 34.9% of FDI stocks as a percentage of GDP during the same year.

Srivastava S. (2004), "Competing for Global FDI: Opportunities and Challenges for the Indian Economy" investigated that impact on FDI inflows to India as a result of increasing competition from another major emerging market economy, i.e., China, in the wake of its accession to the WTO.

Sharma K. (2000), "Export Growth in India: Has FDI played a Role?" Export supply is positively related to the domestic relative price of exports and higher domestic demand reduces export supply. Foreign investment appears to have statistically no significant impact on export performance although the coefficient of FDI has a positive sign.

After reviewing the literature, need is felt to have a descriptive study of FDI as well as FII in India during the period 2000 to 2015. Therefore, firstly prospects of foreign investment, then cost, benefits, role, and trends of foreign investment have been studied, Also, current scenario of foreign investment has also been studied.

Prospects of Foreign Investment in India

India is seriously a compelling story for investors because of the resilient nature of the Indian economy. Many transformations have occurred in the recent past and India is being looked as an opportunity for long term growth instead of short term profit. Despite various problems like political uncertainty, infrastructural deficiencies, and bureaucratic hassles in India, no business whether small or large aiming to become a global player can afford to ignore Indian Market. It has become an optimistic destination for foreign investors. The reasons are: size and growth of India's GDP, exposure to different sectors, demographic dividend, a robust financial sector and quality of investment markets etc. Also the efforts of Indian Government to make India as attractive investment destination for start-ups are appreciable. Department of Industrial Policy and Promotion (DIPP) is dealing with FDI and its related matters. In January 2016, Mr. Modi had unveiled a slew of incentives to boost start-ups like offering a tax holiday and inspector raj-free regime for three years, capital gains tax exemption and Rs 10000 crore corpuses to fund them. And now DIPP is planning to introduce a campaign for financial awareness among domestic and foreign investors.

Cost and Benefits of Foreign Investment Inflows to India

Foreign inflows supplements domestic capital, as well as technology and skills of existing companies. It is helpful in establishing new companies, generating employment opportunities, sharing expertise, back end infrastructure and research and development in host country. FDI challenges the monopoly of certain domestic Indian companies and ultimate benefit goes to Indian consumers. It helps in boosting healthy competition and checking inflation. But the story does not end here. Many voices are against bringing foreign investment in India as it is said that it leads to unfair competition because of dominance of organised retailers. The loss of jobs, loss of self competitive strength is also the costs which Indians can face. But overall when we see the impact of foreign investment flows on GDP of India then ultimately, it can be concluded that benefits of foreign investment flows outweigh the cost of its flows.

Current Scenario

There have been a vast potential in terms of investment opportunities available to foreign investors in India. Hoping to attract more FDI, the government has eased FDI requirements in 15 major sectors. India offers two routes for FDI: the automatic route which does not need pre-approval by the government and the FDI norms under automatic route has been relaxed. In certain sectors where FDI is allowed through automatic route; if it exceeds certain limits, FDI now can enter through second route i.e. government approval route. The Prime Minister Modi Ji has fronted the Make in India program during his official visits to 28 countries in the past 15 months. Thus far, India has received over US 19 billion dollars in FDI in 2014-15 from a dozen major FDI source countries. In all 25 sectors in Make in India Program, a 100 percent FDI has been allowed, with exceptions for space (74 %), defence (49%) and news media (26%). In the automobile industry, automatic approval for foreign equity investment upto 100 percent with no minimum investment criteria, and that manufacturing and imports are exempt from licensing and approvals. The result is that General Motors have announced to invest US $1 billion in its bid to make cars for domestic consumption and export. Although caps still exist in many sectors, they have been raised by 25 to 50 percent in most cases. Additionally, the government has offered tax incentives to encourage investment in India. Among them are: Additional depreciation allowance of 15 percent to manufacturing companies that invest more than $ 1 billion rupees in plant and machinery, Incentives for businesses located in Special Economic Zones, National Investment and Manufacturing Zones, and Special Export Oriented Units, Duty drawback and duty exemption schemes, and also area based incentives along with Sector-specific Incentives. This concludes that India is providing a lot of investment avenues for all.

Trends of Foreign Investment Inflows in India

Table 1: Financial Year-Wise Foreign Investment Inflow Data (2000-01 to 2015-16)

(Amount US $ million)

Financial Year	FDI Flows	FIIs Flows
2000-01	4029	1847
2001-02	6130	1505
2002-03	5035	377
2003-04	4322	10916
2004-05	6051	8686
2005-06	8961	9926
2006-07	22826	3225
2007-08	34843	20328
2008-09	41873	(-)15017
2009-10	37745	29048
2010-11	34847	29422
2011-12	46556	16812
2012-13	34298	27582
2013-14	36046	5009
2014-15	45148(E)	40923(E)

Source: www.dipp.nic.in

Table 1 depicts the trends in FDI and FII as per International Best Practices. FDI includes Equity capital, Re-invested earnings and other capital. And FII flows represent Net FII investment. As is apparent from the above table that the % growth in FDI flows is maximum in the year 2006-07 i.e. (+) 155 % whereas FII flow in India is maximum in the year 2014-15 but in the last quarter of the study it is showing negative trend. And FDI after 2012-13 periods is showing upward trend. This simply indicates that investment through FDI is more in our country than FIIs.

Role and Trends of foreign investment inflows in Indian Economy

After studying the trends of FDIs and FIIs in India, it is needed to analyse the role of investment flows in making stronger economy. The impact of foreign investment flows on GDP of India explains itself its role in boosting the growth of nation. Table 2 depicts the evaluation of FDI and GDP in India for the period starting from 2000-01 to 2014-15.

Table 2: FDI inflows & its Impact on GDP of India

Financial Year	FDI Equity Inflows(in US Million $)	Growth rate of FDI inflow (in $)	Growth rate of GDP	FDI as % of GDP
2000-01	2463	-	-	0.54
2001-02	4065	+65	8.72	0.86
2002-03	2705	-33	7.75	0.55
2003-04	2188	-19	12.03	0.38
2004-05	3219	+47	13.16	0.50
2005-06	5540	+72	14.10	0.72
2006-07	12492	+125	16.60	1.43
2007-08	24575	+97	15.91	2.15
2008-09	31396	+28	15.75	2.70
2009-10	25834	-18	15.18	2.02
2010-11	21383	-17	18.66	1.34
2011-12	35121	+64	15.77	1.97
2012-13	22423	-36	11.88	1.29
2013-14	24299	+8	11.54	1.41
2014-15	30931	+27	10.28	1.64

Source: www.dipp.nic.in , www.rbi.org

It can be seen from the above table that equity investment through FDI is showing increasing inflows in India in most of the years and in some years; particularly after 2007-08, the situation got worsened because of financial crisis but in later years it is seen that easing of norms are making India an investment destination for FDIs. Also, the impact of FDI on Indian GDP can be seen in the table. GDP has grown over the years along with increase in FDIs. Therefore, it can be concluded that role of foreign investment inflows is very important in boosting the growth of the nation. Further, it is important to know the costs and benefits of foreign investments.

Conclusion

We are in the 21st century and we can't ignore the universal trends easily. Inspite of the oppositions by several Indians for FDIs , it would be beneficial for Indian economy to increase the foreign investment inflows further so as to make itself number one in the global trade. The study also concluded with the fact that India is relaxing norms, easing legal formalities, giving more transparency, and speedy and timely grievance redressal mechanism; thereby inducing foreign investors to invest in India and helping in making “Grow India”.

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