ISSN No:-2456-2165

Impacts of Foreign Direct Investment in India

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TOPIC : INDIA'S EFFECTS OF FOREIGN DIRECT INVESTMENT

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OBSERVATIONS FROM THE RESEARCH PROPOSAL

If we encourage FDI in India there will be rapid growth in the gross national product. Even the employment rate will be increasing by rapid growth of FDI in to the Economy. The outsourcing of knowledge form India especially in information technology sector improved the know-how process. FDI has been a booming factor that has bolstered the economic life of India but on the other hand it is also being blamed for outstanding domestic inflows. The present study tries to empirically examine the major factors which have determined the inflow of FDI in India in the post reform period.

ISSN No:-2456-2165

ABSTRACT

This paper is attempted to make an analysis of FDI in India and its impact on growth. It also focuses on the determinants and needs of FDI, year-wise analysis, sectoral analysis and sources of FDI and reasons. One of the economic aspects of globalization is the fact that increasing investments in the form of Foreign Direct Investments. In the recent times due to the global recession most of the countries have not been able to pull investments. India has been able to attract better FDI's than the developed countries even during the crisis period. Especially in the recent years the FDI in India has been following a positive growth rate. Since 1991 the government has focused on liberalization of policies to welcome foreign direct investments. These investments have been a key driver for accelerating the economic growth through technology transfer, employment generation, and improved access to managerial expertise, global capital, product markets and distribution network. FDI in India has enabled to achieve a certain degree of financial stability; growth and development to sustain and compete in the global economy.

ISSN No:-2456-2165

Chapter One
INTRODCUTION

India is the largest democracy and is fourth largest economy (in terms of purchasing power parity) in the world. India with its consistent growth performance and abundant high-skilled manpower provides enormous opportunity for investment, both domestic and foreign. Investment in India can be made both by non-resident as well as resident Indian entities. Any non-resident investing in an Indian company is Foreign Direct Investment (FDI).

The Government embarked upon major economic reforms since mid-1991 with a view to integrate with the world economy, and to emerge as a significant player in the globalization process. Reforms undertaken include decontrol of industries from the stringent regulatory process; simplification of investment procedures, promotion of Foreign Direct Investment (FDI), liberalization of exchange control, rationalization of taxes and public sector divestment. The FDI policy was liberalized progressively through review of the policy on an ongoing basis and allowing FDI in more industries under the automatic route.

A number of studies in the recent past have highlighted on growing attractiveness of India as an investment destination. According to UNCTAD's World Investment Report 2007, India is the second most attractive investment destination for FDI for 2007-09.

India has one of the most liberal and transparent policies on FDI among the emerging economies. FDI up to 100 percent is allowed under automatic route in all activities and sectors except few sectors like manufacturing of cigar and cigarettes of tobacco, electronic aerospace and defense equipments, etc.

FDI policy is reviewed on continuous basis and changes in sectoral polices / sectoral equity cap are notified through press notes by the Secretariat for Industrial Assistance (SIA),Department of Industrial policy and promotion (DIIP).FDI policy is also notified by Reserve Bank of India (RBI) under Foreign Exchange Management Act (FEMA) 1991.

FDI in sectors /activities to the extent permitted under automatic route does not require any prior approval either by the Government or Reserve Bank of India. The investor is only required to notify the Concerned Regional office of RBI within 30 days of receipt of inward remittances and file the required documents with that office within 30 days of issue of shares to foreign investors.

The Government has decided to allow FDI up to 51 percent; with prior Government approval, in retail 'single brand products'. This is inter-alia aimed at attracting investment in production and marketing, improving the availability of such goods for the consumers, encouraging increased sourcing of goods from India, and enhancing competitiveness of Indian enterprise through access to global designs, technology and management practices.

The Government has put in place a liberal foreign technology transfer policy as well. At present, foreign technology collaboration involving payment of lump sum amount of up to US$2 million and/or royalty at the rate of 5 percent on domestic sales and 8 percent on exports are allowed under the automatic route. There are no limits on the duration of royalty payments. In addition, the current policy also allows payment of royalty up to 2% on exports and 1% on domestic sales under the automatic route for use of trademark and brand names of the foreign collaborator without technology transfer. Proposals involving royalty payments beyond the limits under the automatic route are considered for Government approval through the Project Approval Board (PAB). The Government has set guidelines for transfer of ownership or control of Indian companies in sectors with caps from resident Indian citizens to non-resident entities.

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Chapter Two
FEATURES OF FDI IN INDIA

In industries with caps, government/FIPB clearance will be required: A non-resident entity or an Indian corporation is being founded with foreign investment. A non-resident entity controls an Indian corporation that was created with foreign money.

As a result of the transfer of shares to non-resident entities through amalgamation, merger, acquisition, or other means, control of an existing Indian company owned or controlled by resident Indian citizens, as well as Indian companies owned or controlled by resident Indian citizens, will be/is being transferred/passed on to a non-resident entity.

The following advantages will result from the proposed proposals: The proposal would ensure that simple, homogeneous, and uniform procedures for calculating direct and indirect foreign investment are used across sectors, with the exception of those where it is particularly specified by legislation or rules. It would also ensure that establishment/changes in ownership or control of an Indian firm from resident Indian nationals to non-resident entities in sectors with sectoral caps would require Government/FIPB clearance.

India has a young demographic profile, with nearly half of the population under the age of 25, and a high proclivity to consume. Every year, some 20-25 million people join the middle class as their discretionary income rises. This tendency might be exploited to both attract investment and create jobs.

The thought of India being a big player in the global economy appeared distant a decade and a half ago; today, because to the force of FDI, it is a reality. Not only has the world's image of India's future changed in the last five years, but so has our own perception of ourselves. The world has recognised India's "arrival." With the establishment of a social and economic foundation, we no longer talk about India's future; instead, we say, "India's future is India."

Chapter Three
OBJECTIVES OF RESEARCH PAPER

- To determine the numerous factors that influence FDI.
- To identify the various elements that affect FDI.
- To present a sector-by-sector, year-by-year examination of FDI in India..

Chapter Four
PROBLEM DOMAIN

4.1 FDI's disadvantages

1. The disadvantages of foreign direct investment are mostly related to operations, profit distribution, and staff.

2. When the flow of foreign direct investment is negatively affected, the economically backward portion of the host country is always inconvenienced.

3. If the host country has a national secret - something that should not be shared with the rest of the world. It has been noticed that a country's defence has been put at danger as a result of foreign direct investment.

4.Certain foreign policies have been noted on occasion that are not well received by the recipient country's workers. Foreign direct investment can often be harmful to those who are making the investment.

5.High travel and communication costs may be associated with foreign direct investment. Language and cultural differences between the investor's home country and the host country could cause complications in the case of foreign direct investment.

6. There is a possibility that a corporation's ownership will be transferred to a foreign company. As a result, many businesses have reacted with caution when considering foreign direct investment.

7.There has been evidence of significant instability in a particular geographical region at times. This is really inconvenient for the investment.

8. In the case of foreign direct investment, the size of the market and the state of the host country could be key variables. If the host country is not well connected to its more modern neighbours, it will be difficult for investors to succeed.

9.If the host country's government is having trouble attracting foreign direct investment and has less influence over the operations of a company that is a totally owned subsidiary of a foreign company. This has major consequences. The investor is not required to follow the economic policies of the country in which they have put their funds totally. Foreign direct investment has had negative consequences on a country's balance of payments at times.

ISSN No:-2456-2165

Chapter Five
SOLUTION DOMAIN

5.1 A Summary of FDI Benefits

Financial partnerships, technological collaborations and joint ventures, capital markets via Euro issues, and private placements or preferential allotments are the four primary pathways for foreign direct investment into India. Inflows of foreign direct investment (FDI) assist developing countries in building a clear, wide, and successful policy. The environment for investment issues, as well as the people and institutional capacities to carry out the same chevalier.

5.2 Benefits of Foreign Direct Investment:

Attracting foreign direct investment has become a critical component of India's economic development plans. In developing countries, FDI assures a large amount of local capital, production level, and employment prospects, which is a crucial step toward the country's economic growth. FDI has been a booming component that has bolstered India's economic vitality, but it has also been criticised for draining domestic inflows.

5.3 Few regulatory norms in terms of investment patterns are said to have been dropped as a result of FDI. FDI has a transformative effect in most cases. The adoption of a number of well-thought-out and applicable measures will increase the profit ratio from foreign direct investment. Some of the most significant benefits of FDI are:

5.4 Economic growth

This is one of the major sectors, which is enormously benefited from foreign direct investment. A remarkable inflow of FDI in various industrial units in India has boosted the economic life of country.

5.5 Trade

Foreign Direct Investments have opened a wide spectrum of opportunities in the trading of goods and services in India both in terms of import and export production. Products of superior quality are manufactured by various industries in India due to greater amount of FDI inflows in the country.

5.6 Employment and skill levels

FDI has also ensured a number of employment opportunities by aiding the setting up of industrial units in various corners of India.

5.7 Technology diffusion and knowledge transfer

FDI apparently helps in the outsourcing of knowledge from India especially in the Information Technology sector. It helps in developing the know-how process in India in terms of enhancing the technological advancement in India.

5.8 Linkages and spillover to domestic firms

Various foreign firms are now occupying a positioning the Indian market through Joint Ventures and collaboration concerns. The maximum amount of the profits gained by the foreign firms through these joint ventures is spent on the Indian market.

ISSN No:-2456-2165

Chapter Six
IN A DEVELOPING ECONOMY LIKE INDIA, FDI IS ESSENTIAL

Foreign direct investment (FDI) provides a major source of capital which brings with it up-to-date technology. It would be difficult to generate this capital through domestic savings, and even if it were not, it would still be difficult to import the necessary technology from abroad, since the transfer of technology to firms with no previous experience of using it is difficult, risky, and expensive.

Over a long period of time FDI creates many externalities in the form of benefits available to the whole economy which the TNCs cannot appropriate as part of their own income. These include transfers of general knowledge and of specific technologies in production and distribution, industrial upgrading, work experience for the labor force, The introduction of modern management and accounting methods, the establishment of finance related and trading networks, and the upgrading of telecommunications services.

FDI in services affects the host country's competitiveness by raising the productivity of capital and enabling the host country to attract new capital on favorable terms. It also creates services that can be used as strategic inputs in the traditional export sector to expand the volume of trade and to upgrade production through product and process innovation.

Foreign investment can change a country's volume and pattern of trade in various income enhancing directions by shifting its comparative advantages and boosting its competitiveness through technology transfer and the effects of several externalities.

ISSN No:-2456-2165

Chapter Seven
GRAPHICAL REPRESENTATION OF FDI – INDIA

➢ *FDI Inflows In India 1948 To 2010*

Amount of FDI	Mid 1948	March 1964	March 1974	March 1980	March 1990	March 2000	March 2010
In Crores	256	565.5	916	933.2	2705	18486	1,23,378

Source: Kumar 39 1995, various issues of SIA Publication

In India, Reserve Bank of India (RBI) publishes foreign investment data on a monthly basis in the RBI Bulletin, which provides component-wise details of direct investment and portfolio investment. Direct investment comprises of inflows through.

(i) Government (SIA/FIPB) route,
(ii) RBI automatic route,
(iii) NRI and
(iv) Acquisition of shares.

Portfolio investment covers:

(i) GDRs/ADRs
(ii) FIIs and
(iii) Offshore funds and others.

Table 2: FDI, Real GDP, Imports and Exports, Interest rate and inflation

Period	FDI (US $ Mn)	Real GDP ($ Mn)	Imports (US $ Mn)	Exports (US $ Mn)	Interest Rates on Central Government Security of 1 year maturity	Whole Sale Price Index (Base=1993-94)
Mar-93	137	73000	5290	5419	12.51	100
Jun-93	123	75000	5394	5114	12.57	102.3
Sep-93	140	74000	5392	5217	12.59	103.4
Dec-93	131	75000	5607	5320	12.61	106.8
Mar-94	192	78000	6907	6554	12.63	107.2
Jun-94	170	80000	5799	5612	12.67	107.9
Sep-94	303	81000	7022	5991	12.65	108.1
Dec-94	309	80000	7437	6701	12.61	108.5
Mar-95	561	85000	8422	8050	12.2	108.8
Jun-95	471	86000	7992	7144	12.19	109.6
Sep-95	449	85000	9233	7471	12.15	110.3
Dec-95	664	87000	9973	8076	12.1	111.2
Mar-96	549	92000	10576	9235	12.8	114.4
Jun-96	595	91000	9140	8211	13.1	117.9
Sep-96	538	91000	8998	7940	13.4	119.3
Dec-96	831	93000	9522	8042	13.75	121.6
Mar-97	878	94000	11777	9335	13.69	122.9
Jun-97	1164	95000	9509	8146	13.66	124.5
Sep-97	795	95000	9868	8617	13.64	126.2
Dec-97	782	97000	10622	8197	13.45	127.2
Mar-98	821	100000	12412	10438	13.1	128.7
Jun-98	904	100000	9894	7471	12.98	129.1
Sep-98	543	102000	11888	8159	12.79	130.6
Dec-98	365	103000	10269	8638	12.82	132.8
Mar-99	668	108000	10763	8941	12.4	135.4
Jun-99	452	109000	10490	8178	12.18	137.9
Sep-99	648	110000	12618	9461	11.97	139.2
Dec-99	400	111000	12105	9180	11.86	140.7
Mar-2000	667	113000	14749	9945	11.84	141.8
Jun-2000	1085	113000	12781	10370	11.91	143.6
Sep-2000	940	114000	13132	11060	11.82	144.2
Dec-2000	893	115000	13119	10999	11.77	145.3
2001-Mar	1113	118000	11765	11676	10.95	148.4
1-Jun	1204	118000	12808	10362	10.99	150.3
1-Sep	1768	119000	13411	10811	11.04	153.4
1-Dec	1387	122000	12624	10633	10.95	155.7
2002-Mar	1766	123000	13131	12236	10.58	157.1
2-Jun	1666	123000	13759	11947	10.22	158.8
2-Sep	1070	125000	14824	13224	10.09	160.7
2-Dec	1125	127000	15914	12999	9.56	161.3
2003-Mar	1175	133000	16745	14557	9.11	162.5
3-Jun	856	135000	17197	13058	8.58	164.9
3-Sep	1198	135000	17210	14373	8.14	165.2
3-Dec	1094	137000	20527	17070	7.34	166.8
2004-Mar	1174	146000	22604	19374	6.97	169.1
4-Jun	1488	147000	23509	17470	6.21	170.6
4-Sep	1756	147000	25235	18490	5.98	173.4
4-Dec	1353	148000	27439	20528	5.71	175.8
2005-Mar	1390	155000	34588	26568	6.01	179.2
5-Jun	2058	156000	34405	23530	6.05	180.2
5-Sep	1846	156000	36424	24500	6.11	185.3
5-Dec	2312	158000	35961	25048	6.25	187.3
2006-Mar	2685	169000	42829	29305	6.84	189.4
6-Jun	3405	169000	40836	29056	6.97	193.7
6-Sep	4398	170000	47168	32032	7.2	194.2
6-Dec	9848	173000	45521	30225	7.34	195.6

ISSN No:-2456-2165

Table-3: Trade Openness

Period	Imports (US $ Mn)	Exports (US $ Mn)	Trade Openness (% of real GDP)
Mar-93	5289.73	5418.91	14.67
Jun-93	5394.45	5113.55	14.01
Sep-93	5391.68	5216.57	14.34
Dec-93	5607.05	5319.92	14.57
Mar-94	6907.17	6553.71	17.26
Jun-94	5799.22	5611.59	14.26
Sep-94	7021.66	5991.3	16.07
Dec-94	7437.45	6701.47	17.67
Mar-95	8422.17	8049.92	19.38
Jun-95	7991.63	7143.78	17.6
Sep-95	9233.41	7471.06	19.65
Dec-95	9973.2	8075.85	20.75
Mar-96	10576.26	9234.61	21.53
Jun-96	9139.86	8210.64	19.07
Sep-96	8997.84	7939.62	18.61
Dec-96	9522.27	8041.75	18.89
Mar-97	11777.11	9335.14	22.46
Jun-97	9509.14	8145.94	18.58
Sep-97	9867.79	8617.42	19.46
Dec-97	10621.68	8196.54	19.4
Mar-98	12411.73	10437.65	22.85
Jun-98	9893.65	7471.14	17.36
Sep-98	11887.83	8158.64	19.65
Dec-98	10269.17	8638.38	18.36
Mar-99	10763.03	8941.06	18.24
Jun-99	10490.02	8177.84	17.13
Sep-99	12617.52	9461.34	20.07
Dec-99	12105	9179.57	19.18
Mar-2000	14748.75	9944.6	21.85
Jun-00	12781.09	10369.71	20.49
Sep-00	13132.32	11059.64	21.22
Dec-00	13119.1	10999.15	20.97
2001-Mar	11764.68	11675.83	19.86
1-Jun	12808.13	10361.77	19.64
1-Sep	13411.17	10811.38	20.36
1-Dec	12623.99	10633.26	19.06
2002-Mar	13130.5	12235.85	20.62
2-Jun	13759.02	11946.66	20.9
2-Sep	14823.68	13223.81	22.44
2-Dec	15914.26	12998.59	22.77
2003-Mar	16745.25	14556.76	23.54
3-Jun	17196.64	13058.23	22.41
3-Sep	17210.33	14373.45	23.4
3-Dec	20527.2	17070.09	27.44
2004-Mar	22603.52	19374.23	28.75
4-Jun	23509.16	17469.75	27.88
4-Sep	25234.8	18490.25	29.74
4-Dec	27439.16	20528.16	32.41
2005-Mar	34588.26	26568.05	39.46
5-Jun	34405.2	23530.21	37.14
5-Sep	36424.11	24499.77	39.05
5-Dec	35961.08	25047.95	38.61
2006-Mar	42828.89	29304.95	42.68
6-Jun	40836.43	29056.24	41.36
6-Sep	47168.18	32031.61	46.59
6-Dec	45520.99	30224.67	43.78

A study by Ana Marr (1997), reviews the recent evidence on the scale of FDI to low-income countries over the period 1970- 96 and major factors determining foreign companies' decisions to invest in a particular country. The paper concludes that large market size, low labor costs and high returns in natural resources are amongst the major determinants in the decision to invest in these countries. China, as a major emerging market, has attracted significant flows of FDI, to become the second largest receipt. Shaukat Ali and Wei Guo (2005) briefly examine the literature on FDI and focuses on likely determinants of FDI in China. They analyze responses from 22 firms operating in China on what they see as the important motivations for them to undertake FDI. Results show that market size (in terms of GDP) is a major factor for FDI especially for the United States firms. For local, export-orientated, Asian firms, low labor costs are the main factor.

ISSN No:-2456-2165

CHAPTER EIGHT
DISCUSSION AND RESULTS

As explained in the table output, the dependent variable in the regression s FDI and the independent variables are real GDP, previous period FDI, previous period GDP, trade openness, interest rates, and WPI. the results show that FDI is explained close to 86% by the independent variables included in this study. the durbin watson value is close to 2 which imply that there exist no autocorrelation into the data. real GDP and previous period FDI are important factors in attracting the FDI inflows in India during the post reform period. previous period FDI and level of inflation in the economy or price stability have significantly contributed in explaining the inflow of FDI. while previous period FDI is positively influences the FDI, inflation in the economy negatively affects the FDI inflows. however, real GDP has positive influence on FDI and is statistically significant at 10 percent significance level. however, trade openness, interest rates and economic growth in the previous period are not important factors in explaining FDI inflows in India.

ISSN No:-2456-2165

CHAPTER NINE
CONCLUSION

Foreign direct investment (FDI) is critical to an economy's growth. Many factors influence FDI inflows into a country, according to the literature, including market size, inflation, trade openness, interest rate, wage rate, business environment, and so on. The current study looked at the factors that influenced FDI inflows into India after the reforms. Our findings reveal that FDI is positively associated to real GDP and previous period FDI inflows, but inversely related to inflation. It was discovered that macroeconomic instability in terms of inflation was a significant factor influencing FDI inflows into India during the post-reform period.

Foreign Direct Investment (FDI) is regarded as the lifeblood of economic development, particularly in developing and developing countries. Multinational corporations (MNCs) take advantage of international commercial prospects by investing in real assets (such as land, buildings, or existing plants) in other nations. MNCs make joint ventures with overseas companies, buy foreign companies, and create new foreign subsidiaries. It is critical to a country's long-term growth, not only as a source of capital, but also for improving the local economy's competitiveness through technology transfer, infrastructural improvements, increased productivity, and the creation of new job opportunities (Deutsche Bundesbank, 2003). MNCs want to increase income through FDI by attracting new sources of demand and creating successful partnerships.

In India, FDI is viewed as a development instrument that can assist in reaching economic self-sufficiency in a variety of industries. Huge incentives and privileges were offered for the influx of foreign capital into India with the launch of the Industrial Policy in 1991. India is a developing country with plenty of room for both consumer and capital products. India's diverse natural resources, stable economic policies, favourable market circumstances, and highly qualified human resources make it an ideal destination for foreign direct investment.

According to a recent poll conducted by the United Nations Conference on Trade and Development (UNCTAD), India will be the third largest recipient of FDI for the three-year period ending in 2012. (World Investment Report 2010). According to the report, services, telecommunications, construction activities, and computer software and hardware drew the most FDI. India liberalised its heavily controlled FDI system in 1991. Controls on international commerce and FDI were significantly reduced in tandem with the effective dismantling of the industrial licencing system. FDI inflows grew after the changes during the post-reform period. In comparison to most other developing countries, India receives a small amount of foreign direct investment.

ISSN No:-2456-2165

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