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Performance of Foreign Direct Investment (FDI) In India: An Investigation

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Abstract

Foreign Direct Investment (FDI) plays very important role in the overall development of any country including India. Its importance lies in the fact that it is non-debt creating foreign capital resources. It may engender benefits by bringing latest technology, skill development, new employment and spillovers. On the other hand Outward Direct investment (ODI) offers an additional path for developing country like India to link up to global markets and production systems. Healthy flow of direct investments, either inward or outward, reflects increasing integration of an economy with the rest of the world. The relationship between FDI and economic growth has long been a subject of great curiosity in the field of international development. Meagerness of foreign direct investment retained many countries as poor country. Keeping in above backdrop, present study is a humble attempt to analyze the FDI inflows in Indian economy in the form of growth rate, sectors attracting the highest FDI, its performance and to draw policy implications flowing from the study.

Key-Words: FDI Inflows, Performance, Sectors, India.

I. INTRODUCTION

Foreign Direct Investment (FDI) plays multidimensional role in the developing world as it has considered a growth enhancing factor in developing countries like India. The relationship between Foreign Direct Investment (FDI) and economic growth has long been a issue of great concern. There are two type of flow of FDI i.e. inflows and Outflows. FDI Inflows helps transfer and improves technology; enhance skills and managerial capabilities. It also provides competitive edge to country's exports improves efficiency as well as quality of services & goods and helps to create employment opportunities. It is mostly preferred source of external finance for the reason that they are not debt creating as well as non-volatile in nature and their returns relay on the projects financed by the investor. Healthy flow of direct investments, either inflows or outflows, reflects increasing integrity of an economy with the rest of the world. A significant objective to promote FDI in any developing country in general and India in particular has been to increase efficiency in production and increase exports. Keeping in above backdrop, we will analyze the FDI inflows in Indian economy. Section II is dedicated on the review of literature on the present issue. Section III describes the objectives of the study & methodology. Section IV analyzes the FDI in flows in India, Performance of FDI inflows will be examined in section V. And lastly, Section VI concludes the study with policy implications.

II. LITERATURE REVIEW

There is no dearth of literature on the present issue. Review of various studies available on FDI reveals that foreign investment is still a matter of debate that whether FDI is boon or bane for host countries economic growth and development? Opinions are still divided. FDI has its own merits and demerits. To justify the need of present study, following literature has been reviewed:

Bhrambhatt et. al. (1996) in his study have identified four major weaknesses (inadequate macroeconomic policies, high levels of protection, inefficient transportation and communications infrastructure and poorly equipped and inflexible labour) depress Indian firms and FDI investors from focusing on export market. They contend that FDI can help to increase the private investment without incurring additional debt and can help relax key infrastructure constraints. Bajpai and Sachs (2000) identified the issues and problems associated with India's present FDI regimes, and more importantly the other associated factors responsible for India's unattractiveness as an investment location. They examine that India's performance in attracting FDI flows have been far from satisfactory. They concluded that a controlled FDI regime, high import tariffs, exit barriers for firms, stringent labor laws, centralized decision making processes, poor quality infrastructure and limited scale of export processing zones make India an unattractive investment location. Kumar (2001) stated that Foreign Direct Investment (FDI) has emerged as the most important source of external finance for developing countries. Chakraborty and Basu (2002) in their study applied co-integration and an error-correction model to examine the link between FDI and economic growth in India and find that GDP in India is not Granger caused by FDI, and the causality runs more from GDP to FDI. V.N Balasubsramanyam and Vidya Mahambre (2003) in their study of FDI in India conclude that FDI is a very good means for the transfer of technology as well as knowhow to the developing countries. They agree with the advocacy of the policies designed to eliminate various sorts of distortion in the product and factor markets. These are policies which should be adopted for both the domestic and foreign investment. Lee (2005) argued that foreign direct investment along with trade liberalization is the key for economic development. Herzer et al. (2007) has argued that with 28 developing countries data there is no long-term &short-term effect of FDI on growth; in fact, there is not a single country having positive unidirectional long-term effect from FDI to GDP. Chakrabory and Nunnenkamp (2008) analyzed sectoral growth impact of FDI on Indian economy. They found that FDI in the service sector appears to have promoted growth through cross-sector spillovers in the manufacturing sector and ultimately results to economic growth. Gohou and Soumare (2010) assess the impact of Foreign Direct Investment (FDI) on welfare across African regions. They uses human development index (HDI) and real per capita GDP. As FDI measure, they use per capita FDI net inflows, FDI net inflows over GDP and FDI net inflows over gross capital formation (GCF). They found that there is a strong positive relationship between FDI and welfare at the aggregate Africa level. However, when taken at the regional level, the impact of FDI on welfare is no longer obvious and differs across regions. Goel M. M. & Walia Ritu K. (2013) in his study analyzed the growth and performance of FDI in Indian economy through country wise, sectoral and total FDI inflows of FDI. Study also examined the relationship between FDI and economic growth and concluded that FDI promotes economic growth significantly.

It is also evident from the above literature that FDI proves to be an engine of economic growth in any country in general and India in particular. In light of above literature, the present paper is a humble attempt to analyze flow of FDI in Indian economy and suggest policy measures to boost flow of FDI to India and from India.

III. OBJECTIVES & RESEARCH METHODOLOGY

The present paper is a humble attempt to analyze the performance of FDI in Indian economy. The specific objectives of the study can be enumerated as follows:

- To analyze the growth trend of FDI inflows in India.
- To explore the country wise FDI inflows in India
- To study the sectoral distribution of FDI inflows in India
- To find out the of FDI Inflows Performance Index of India.

The present study is of analytical in nature and exclusively based on secondary data which has been collected from the various issues of Handbook of Statistics on the Indian Economy and Reserve Bank of India Bulletin published by Reserve Bank of India (RBI). The study considers the time period from the year 1991 onwards. To examine the Foreign Direct Investment in India, the available data have been processed and presented in suitable tables and graphs and percentage growth rate of FDI is computed.

To judge the performance of FDI, the FDI performance index is calculated. This index is developed by the UNCTAD to measure a country's relative position in the world in terms of FDI performance. Formally, it is the ratio of a country´s share in global FDI flows to its share in global GDP and can be calculated as follows:

$$\text{FDI Performance Index}_{\,i} = \frac{FDI\text{i}/FDI\text{world}}{GDP\text{i}/GDP\text{world}}$$

If a country's share of global inward FDI matches its relative share in global GDP, the country's Inward FDI Performance Index is equal to one. A value greater than one indicates a larger share of FDI relative to GDP indicating that one attract more FDI than could be expected on the basis of their relative GDP size, a value less than one indicates a smaller share of FDI relative to GDP. A negative value means foreign investors disinvested in that period. To calculate performance index data from UNCTAD has been used.

IV.FOREIGN DIRECT INVESTMENT INFLOWS IN INDIA

India followed a fairly preventive foreign private investment policy until 1991 - relying more on bilateral and multilateral loans with long maturities. With the introduction of economic reforms (1991) in the form of liberalization, globalization and privatization, there has been a paradigm shift in FDI inflows in India. Thus, there is a global race to attract foreign funds through this route. Over the years FDI inflows in India has been increasing. As shown in table no 1 cumulative inflows of FDI in India from April 2000 to March 2017 is US $ 484,351million and inflows of FDI equity is US $ 331,991 Millions.

TABLE 1: TOTAL FDI INFLOWS (FROM APRIL, 2000 TO MARCH, 2017)

Cumulative Amount of FDI Inflows (Equity inflows + Re-invested earnings + other Capital)	**US $ 484,351 Million**
Cumulative Amount of FDI Equity Inflows (Excluding, amount remitted through RBI's-+NRI Schemes))	**US $ 331,991 Million**

Source: *Government of India (GOI), FDI Statistics, Department of Industrial Policy and Promotion*

Investment opportunities in India are high at present time. The factors that attracted investment in India are stable economic policies, availability of cheap and quality human resources, and opportunities of new unexplored markets. As a result of which investors are showing their growing confidence in the immediate and medium term prospects of the Indian economy.

In this regard the FDIinflow in India from the year 1991-92 has been shown in the table 2. It was $ 165 Million in 1991-92 and increasedto US $ 60082 millionin March 2017. Percentage growth over previous year is also shown in table 2. It is highest in year 2006-07.

TABLE 2: FDI INFLOWS IN INDIA FINANCIAL YEAR WISE

Year	FDI Inflows (US $ Million)	%age Growth over Previous Year
1991-92	165	-
1992-93	393	138.18
1993-94	654	66.41
1994-95	1374	110.09
1995-96	2141	55.82
1996-97	2770	29.38
1997-98	3682	32.92
1998-99	3082	-16.30
1999-00	2439	-20.86
2000-01	4029	65.19
2001-02	6130	52.15
2002-03	5035	-17.86
2003-04	4322	-14.16
2004-05	6051	40.00
2005-06	8961	48.09
2006-07	22826	154.72
2007-08	34843	52.65
2008-09	41873	20.18
2009-10	37745	-9.86

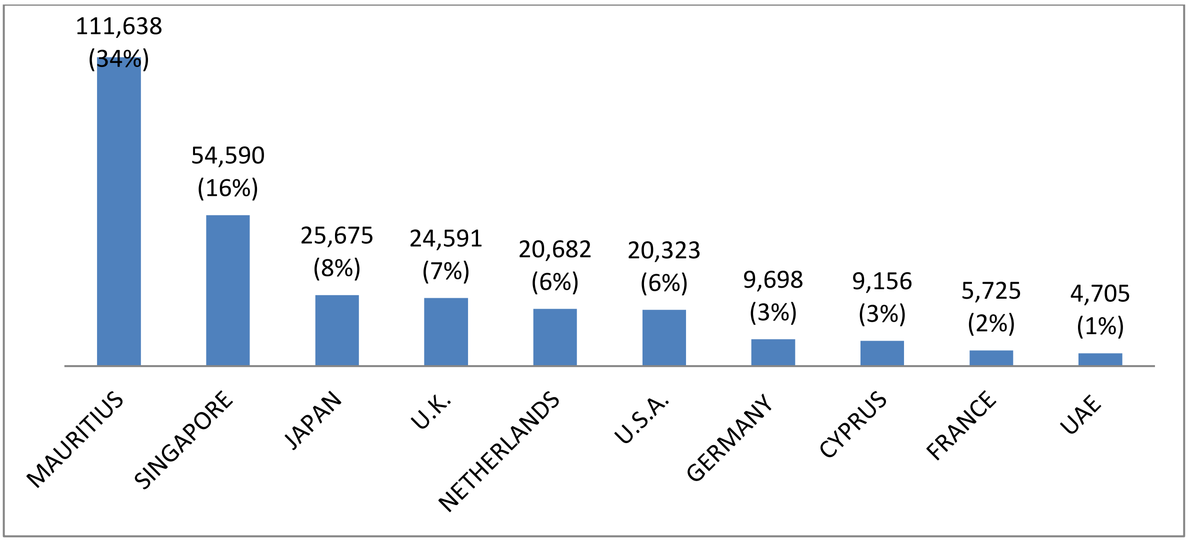
2010-11	34847	-7.68
2011-12	46556	33.60
2012-13	34298	-26.33
2013-14	36049	25.24
2014-15 (P)	45148	23.99
2015-16 (P)	55559	22.83
2016-17 (P)	60082	8.0

Source: *Economic Survey, GOI, & SIA Newsletter (various FDI fact sheets).*

Percentage growth rate of FDI inflows has slowed down in 2016-17 which may bedue toslowing economic growth and falling commodities prices weighed on FDI flows to developing economies (UNCTAD, Feb 2017).There are fluctuations in FDI inflows, which may be due to the effect of global economic slowdown. As our economy has adopted some safeguard policies so after some time there is positive growth in FDI inflows.Various studies have projected India among top five favored destinations for FDI. Figure 1 presents the share of majorinvesting countries in India. It is found that Mauritius emerged as one of thelargest foreign investors in India. Upto March 2017, 86 per cent of FDI inflows in India is contributed by these ten countries while remaining 14 percent by rest of the world. Country wise FDI inflows to India are dominated by Mauritius (34%), followed by Singapore (16%), Japan (8%), U.K. (7%),, Netherlands and U.S.A. (6%), Germany and Cyprus (3%), France (2%), UAE (1%).

FIGURE 1: COUNTRYWISE FDI EQUITY INFLOWS IN INDIA

(Cumulative Inflow from April 2000 to March 2017 in US $ Million)



Note:() are percentages of FDI to total FDI inflow in India*

Source :*Government of India (GOI), FDI Statistics, Department of Industrial Policy and Promotion*

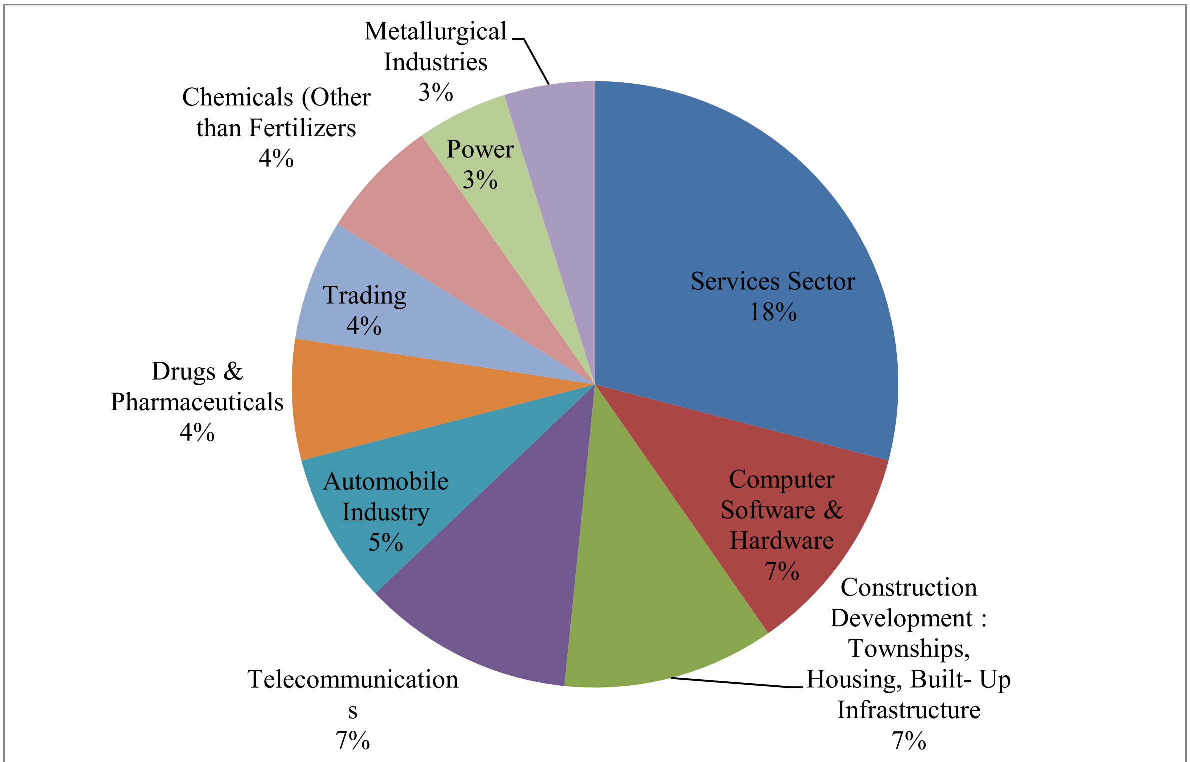
It needs to be pointed out that the FDI inflows from Mauritius to India are misleading. This is so because Mauritius has low rates of taxation and agreements between India on double tax avoidance regime. In order to get benefits out of the low tax agreement between Mauritius and India. Large number of foreign firms and even some Indian firms started dummy companies in Mauritius, and then invested in India via Mauritius.

Sectoral distribution of FDI equity inflows is shown in figure 2. Based upon the data there are sixty three sectors in which FDI inflows are seen but top ten industries attract almost 62 per cent of FDI equity inflows. However, from April 2000 to March 2017, service sector has been the highest contributor of FDI inflows to India (18%), followed by Computer software & hardware (7%), construction development (7%) , Telecommunication (7%), Automobile Industry (5%), Drugs & Pharmaceuticals (4%), Trading (4%), Chemicals (other than fertilizers (4%), Power (3%), , Metallurgical industries (3%).

The main reason in highest investment in service sector is due to low cost wages and wide demand-supply gap in financial services particularly in banking, insurance and telecommunication. Gradually India has become important Centre for back-office processing, call centers, technical support, medical transcriptions, knowledge process outsourcing (KPOs), financial analysis and business processing hub for financial services and insurance claims.

FIGURE 2: SECTORS ATTRACTING HIGHEST FDI EQUITY INFLOWS

(Percentage to Total FDI Equity Inflows, April 2000 to March2017)



Source: *Government of India (GOI), FDI Statistics, Department of Industrial Policy and Promotion*

V. PERFORMANCE OF FDI IN INDIA

The Government of India has taken an inclusive review of the FDI policy and allied procedure recently. Many measures have been initiated to improve the performance of FDI. The FDI inflows performance index is shown in table 2. It is clear from the table that FDI performance index is very low in 1991.over the period of time, as government adopts favorable policies towards FDI it improves. It is clear from the following table that FDI inflows continue increase up to 1997 and down during 1998 to 2000 and improves again 2000 onwards.

It is lowest in 2009; the reason may be global economic slowdown/crisis and later starts improving again. It was greater than 1 in 2010 and 2014, showing attractive destination for foreign investors. Large market size and potential, low wage cost and availability of skilled labour force in India are the main key for attracting foreign investors.

TABLE 2: FDI INFLOWS PERFORMANCE INDEX SINCE 1991

Year	Performance Index
1991	0.04
1992	0.13
1993	0.22
1994	0.33
1995	0.53
1996	0.53
1997	0.56
1998	0.28
1999	0.14
2000	0.19
2001	0.55
2002	0.65
2003	0.51
2004	0.52
2005	0.46
2006	0.79
2007	0.65
2008	0.61
2009	0.06
2010	1.34
2011	0.87
2012	0.67
2013	0.75
2014	1.06

***Source**: Authors Calculation based on UNCTAD data.*

VI. CONCLUSION WITH POLICY IMPLICATIONS

In brief, the present paper makes an analysis of growth and performance of FDI in Indian economy through examining country-wise, sectoral and total inflows of FDI. The study confirms that Mauritius, Singapore, Japan, U.K., Netherlands are top five nation contributing highest share in FDI equity inflows in India. In terms of sectoral share, the services sector is enjoying first place in attracting FDI inflows. Therefore, FDI is necessary for creation of jobs, expansion of existing manufacturing industries and development of the new one. Indeed, it is also essential in the healthcare, education, infrastructure development, R&D, retailing and in long-term financial projects. We should welcome the inflow of foreign investment because it enable us to achieve our cherished goal like making favorable the balance of payment, rapid economic development, removal of poverty, and internal personal disparity in the development and also it is very much convenient and favorable for Indian economy. It is clear from the study that FDI inflow performance index for Indian economy has improved over the time period. But India is lacking behind china. Government must pay attention to attract FDI to improve the health of different sectors of Indian economy. It is also said that the government must promote sustainable development through FDI by further strengthening of quality education, healthcare facilities and R&D system, political involvement of people and by ensuring personal security of the citizens in the country.

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