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FOREIGN DIRECT INVESTMENT IN INDIAN ECONOMY

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ABSTRACT

Foreign Direct Investment is nothing but the investment made by a company in one country into the business of another company in another country. The basic aim for this is to gain monetary benefits and to access the management of ownership of that company. The benefit for the company welcoming FDI is that they have a better technology, more pool of funds to expand business as well as more employment opportunities. Thus, the paper analyzes the sector-wise and country-wise of FDI Inflow in Indian Economy. The paper focus on the trend of FDI Inflow from past 25 years. The paper will further examine the impact of FDI on Indian Economy. Finally, the paper analyses the data and concludes some key findings and suggestions.

KEYWORDS- *FDI, Indian Economy, Foreign Direct Investment, Economic growth*

INTRODUCTION

Foreign Direct Investment is nothing but the investment made by a company in one country into the business of another company in another country. The basic aim for this is to gain monetary benefits and to access the management of ownership of that company. The benefit for the company welcoming FDI is that they have a better technology, more pool of funds to expand business as well as more employment opportunities. It simply involves ownership and control in a foreign country of a foreign company.

Foreign Direct Investment (FDI) is nothing but a form by which an entity of one country can control and manage ownership of a business in another country. It helps the investing companies to expand its business base and reap the benefits of economies of scale. It helps the other companies in which the investment is made to have better flow of investment, technology and profits. It can be invested by two modes- Greenfield and Brownfield Investment.

In Indian Economy, mostly FDI flow is in form of brownfield investment thus there are more mergers and acquisitions. FDI flow in India increased from US $97 million (1991) to US $36,008 million (2015-16) which is more than 35,000 times. According to Department of for Promotion of Industry and Internal Trade (DPIIT), FDI will be valued US $33,492 million between April 2000 and December 2018. FDI in India is majorly contributed by Mauritius and Singapore in absolute terms but in comparison to increase in the amount of percentage as compare to earlier years the major contributor is Cayman Islands and Canada.

Since FDI is among one of the most debatable and crucial topics thus the study is focused on examining the impact of FDI.

BACKGROUND

History of foreign investment in India can be traced back with the establishment of Britain's East India Company. British capital came into India during colonial period. British companies set up their units in the sectors which suited their economic and business interest like mining sector etc. Before independence major amount of foreign investment came from British Companies. After independence, India became a Mixed Economy but controlled wholly or substantially the whole by the Government.

A Mixed economy is an economic system which blends elements of the market economies with the planned economies, in other words in this system free markets coexist with state interventions in some areas usually in public services, defense, and infrastructure and basic industries. All modern economies where the means of production are shared between the private and public sectors are mixed which is also known as Dual Economy.

Prior to 1991, Indian Economy suffered from various economic problems. Some of them were huge fiscal and revenue deficits, adverse Balance of Payments (BOP) and Balance of Trade (BOT), Sick Public Sector Undertakings (PSUs), defer and default in payment of Foreign borrowing by Government etc. In October 1990, World Bank's Report advocated a 20 percent devaluation of rupee to correct the balance of payments problem. In 1991, the country experienced a balance of payment dilemma following the Gulf

War and the downfall of the erstwhile Soviet Union. Thus, Narasimha Rao and Manmohan Singh set out redeem for crisis and proposed the New Economic Policy, 1991.

In beginning of July 1991, economy shifted to Mixed Economy with redefined role of state. The committee introduced New Economic Policy - Liberalisation, Privatisation and Globalisation (LPG) as major economic reforms which resulted in equal control and opportunities for Private enterprises. Primary objective of these reforms was to make the economy of India the fastest developing economy on the globe with capabilities that help India to match with various developed economies.

Foreign Direct Investment is the outcome of this New Economic Policy which helps to increase the productive capacity of the economy.

REVIEW OF LITERATURE

Sahoo (2004) investigated in his thesis named ***'An Analysis of the Impact of Foreign Direct Investment on the Indian Economy'*** the trends, growth and patterns of FDI inflows and determinants of FDI along with their impact at macro and sectoral level. The study stated that at macro level, FDI has a positive relationship in economic growth in India. At sectoral level FDI in major sectors has a positive impact in increasing the output, labour, productivities and exports but the major sectors have little variation in overall impact.

Hooda (2011) elucidated in her thesis ***'A Study of FDI and Indian Economy'*** the trends and pattern of FDI in India, assess the determinants of FDI Inflows in India and Impact of FDI on Indian Economy. The study concluded that FDI have a positive effect on Exchange rate, TradeGDP, Foreign Exchange Reserves (ReservesGDP) and Gross Domestic Product Growth (GDPG) and negative impact on Research & Development.

Kumar (2016) investigated in his thesis named ***'Impact of FDI on Economic Growth in India'*** trends of FDI in India, regional trends, major investors of FDI in India and impact of FDI on macroeconomic indicators which included GDP, Export, Import, Foreign Reserve, GCF, Per-capita Income and Gross Domestic Savings. The study states that there FDI has a positive impact on various indicators both on account of OLS Estimation and Econometric evaluation techniques and is satisfactory.

Khatoon (2016) examined in the article named "***A Study of Growth of Foreign Direct Investment in Different Sectors of Economy- A Descriptive and Analytical study***" the growth of FDI Equity Inflows Year-Wise, Sector-Wise and Country-Wise. The article concluded that FDI plays an important role in boosting employment opportunities, formation of capital, eccess to new technology etc.

Choi and Baek (2017) studied in their article "***Does FDI Really Matter to Economic Growth in India?***" the productivity spillover effects from FDI Inflow in India. They created a model linking productivity in India with FDI with GDP being the major determinant. After running the viability of model, they concluded that FDI is found to engine for economic growth in India but more depth analysis of sector or industry should be done.

OBJECTIVE OF THE STUDY

The paper uses an exploratory research technique based on past literature from respective journals, reports, newspapers and magazines covering wide collection of academic literature on medical tourism. The objectives of the paper are:

- To review the background of Indian Economy
- To study the trend of FDI flow in Indian Economy
- To examine sector-wise flow of FDI in India
- To look into the industry-wise flow of FDI in India
- To analyze the impact of FDI on Indian Economy

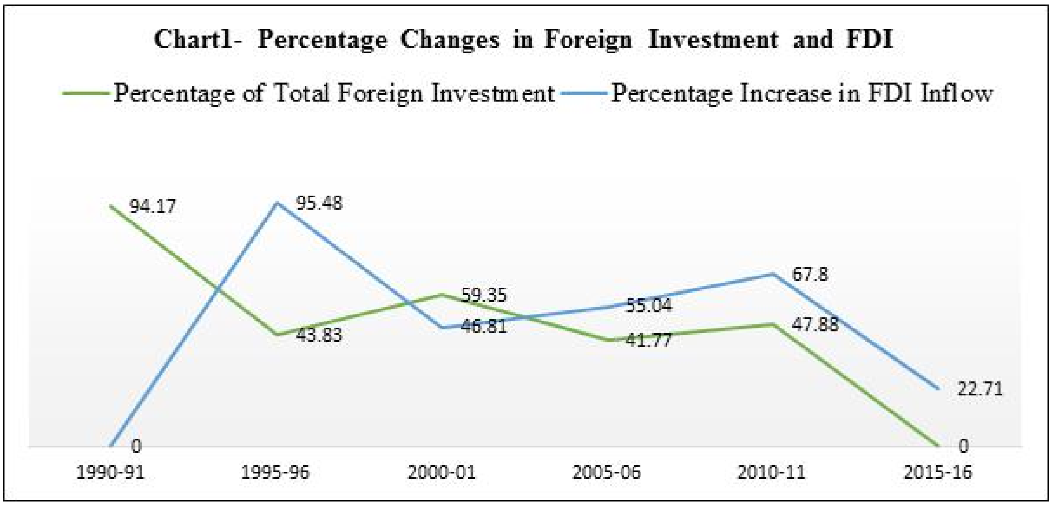
FDI INFLOW IN INDIA

FDI is one of the major sources of capital, technology and management in India. It is assumed to be one of the prime reasons for rapid growth in the economy after the implication of New Economic Policy. Thus, this section focusses on the amount of FDI Inflows in India since LPG. It can be seen from the table that FDI in India is increasing every year and it has increased from US $97 million to US $36008 million post liberalization.

Table 1 - Percentage Changes in Foreign Investment and FDI

Year	Foreign Direct Investment (FDI) (in US $ Million)	Percentage of Total Foreign Investment	Percentage Increase in FDI Inflow
1990-91	97	94.17	-
1995-96	2,144	43.83	95.48
2000-01	4,029	59.35	46.81
2005-06	8,961	41.77	55.04
2010-11	27,829	47.88	67.80
2015-16	36,008	-	22.71
Source*- Datt & Sundharam's Indian Economy (72nd Edition) and various other sources*			

It can be further analyzed from the above chart that from the past 25 years percentage increase in foreign investment and FDI has no direct relationship as percentage increase in FDI keeps on fluctuating sometimes at increasing rate sometimes at diminishing rate depending upon the economic condition of the country and world. It implies that as a matter of policy, the host country can depend on regular inflow of FDI if it creates a conducive climate for the purpose.



SECTOR-WISE FDI IN INDIA

According to the data it is observed that there has been significant amount of increase in the amount of FDI Inflow from 2013-14 to 2016-17 in all industries except Real Estate and Trading. The provisional data provided by RBI for the year 2017-18 showcase that there has been decline in FDI in Miscellaneous services and Others by 12.7% and 29.64% respectively as compared to 2013-14. In 2017-18, maximum growth in FDI Inflow is seen in Real Estate Activities, i.e., 74% as compared to 2016-17. The major decline is seen in industries such as Miscellaneous services, Others, Mining, Manufacturing and Construction by 117%, 108%, 72%, 69% and 22% respectively. The trading industry is sluggish since 2015-16 as there has been no FDI inflow in the industry. In comparison to 2013-14, the maximum growth of 85.74% is observed in Communication services followed by Business Services with 82.66%.

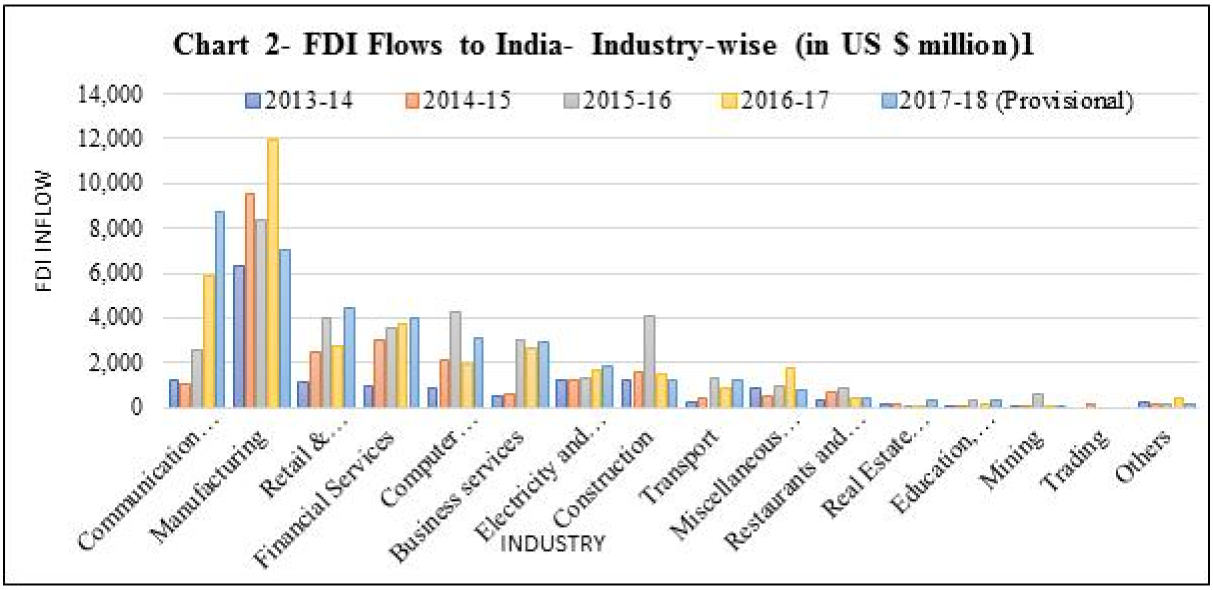


Table 2- FDI Flows to India- Industry-wise (in US $ million)					
Industry	**2013-14**	**2014-15**	**2015-16**	**2016-17**	**2017-18 (Provisional)**
Communication Services	1,256	1,075	2,638	5,876	8,809
Manufacturing	6,381	9,613	8,439	11,972	7,066
Retail & Wholesale Trade	1,139	2,551	3,998	2,771	4,478
Financial Services	1,026	3,075	3,547	3,732	4,070
Computer Services	934	2,154	4,319	1,937	3,173
Business services	521	680	3,031	2,684	3,005
Electricity and other energy Generation, Distribution & Transmission	1,284	1,284	1,364	1,722	1,870
Construction	1,276	1,640	4,141	1,564	1,281
Transport	311	482	1,363	891	1,267
Miscellaneous Services	941	586	1,022	1,816	835
Restaurants and Hotels	361	686	889	430	452
Real Estate Activities	201	202	112	105	405
Education, Research & Development	107	131	394	205	347
Mining	24	129	596	141	82
Trading	0	228	0	0	0
Others	293	232	215	470	226

Source: *RBI*

Note- Includes FDI through SIA/FIPB and RBI routes only.

In absolute terms, increase in the Manufacturing sector from 2013-14 to 2017-18 was US $7,553 million as compared to Retail and Wholesale trade which was US $3,339 million. Miscellaneous services and Others observed a significant amount of decrease, i.e., US $106 and US $67 million respectively. There has been huge decrease in FDI Inflow from 2016-17 to 2017-18 in manufacturing sector amounting US $4906 million followed by construction and mining with amount of US $283 and US $59 million respectively. Communication Services Industry is the most benefited sector in terms of FDI Inflow, there has been an increase of US $2933 million from 2016-17 to 2017-18.

COUNTRY-WISE FDI INFLOW IN INDIA

According to the table it can be deduced that the major contributor of FDI Inflow in India is Mauritius with an increase of US $9720 million from 2013-14 to 2017-18 followed by Singapore with US $4,858 million. Japan and Cyprus observed a decline in FDI Inflow amounting US $482 and US $256 million respectively. As compared to 2016-17, India received maximum increase in FDI from Singapore (US $2744 million) in 2017-18. The country with the major disinvestment is India is Japan with amount of US $2924 million.

Table 3- FDI Flows to India- Country-wise (in US $ million)					
Country	**2013-14**	**2014-15**	**2015-16**	**2016-17**	**2017-18 (Provisional)**
Mauritius	3,695	5,878	7,542	13,383	13,415
Singapore	4,415	5,137	12,479	6,529	9,273
Netherlands	1,157	2,154	2,330	3,234	2,677
USA	617	1,981	4,124	2,138	1,973
Japan	1,795	2,019	1,818	4,237	1,313
Cayman Islands	25	72	440	49	1,140
Germany	650	942	927	845	1,095
Hong Kong	85	325	344	134	1,044
United Kingdom	111	1,891	842	1,301	716
Switzerland	356	292	195	502	506
UAE	239	327	961	645	408
France	229	347	392	487	403
China	121	505	461	198	350
Italy	185	167	279	364	308
South Korea	189	138	241	466	293
Cyprus	546	737	488	282	290
Canada	11	153	52	32	274
Others	1,626	1,682	2,243	1,490	1,889

Source: RBI

Note- Includes FDI through SIA/FIPB and RBI routes only.

In terms of percentage, maximum increase in investment in FDI Inflow is done by Cayman Islands with 97.81% followed by Canada (95.98%) and Hong Kong (91.86%) from 2013-14 to 2017-18. Japan and Cyprus are among the major countries to disinvest in FDI in India in 2017-18 as compared to 2013-14, with the percentage of 36.7 and 88.3 respectively.As compared to 2016-17, Japan showed more than double decline in the FDI with 222% followed by United Kingdom with decline of 81.7%. The country which almost doubled their investment this year is again Cayman Islands with an increase of 95.7% followed by Canada (88.32%).

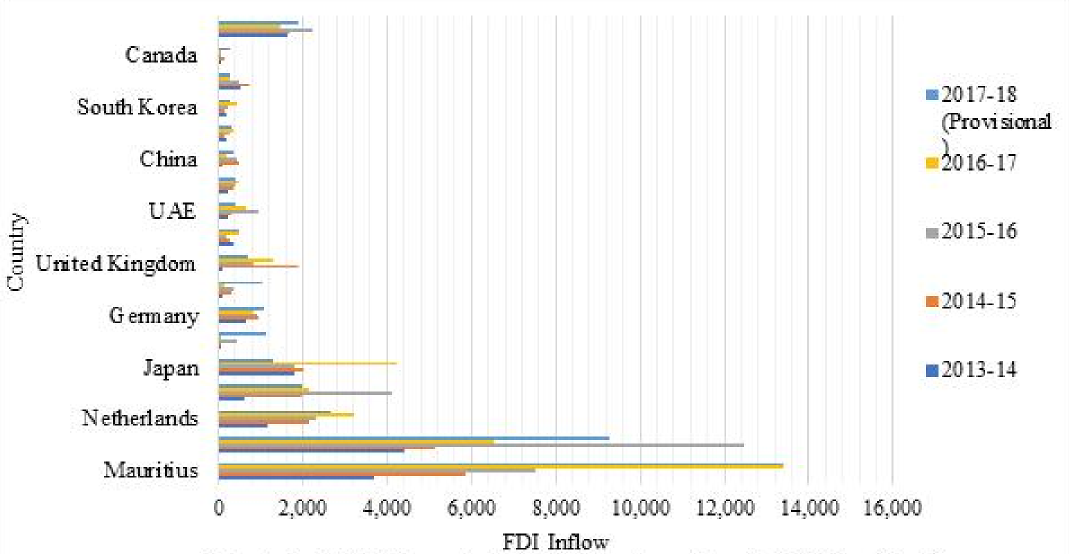


Chart 3 - FDI Flows to India- Country-wise (in US $ million)

FDI IN INDIAN ECONOMY

Trend of FDI and Macroeconomic Indicators in Indian Economy-

It can be summarized from the table below that trend of FDI is very fluctuating it keeps on decreasing or increasing. It is least in the year 2006-07 amounting 2,289 crores just before the fall of the world economy. It shows the highest rise in the year 2005-06. All other macro-economic indicators except REER keeps on increasing. REER fell in the year 2008-09 just after the great depression in 2008.

Table 4- Trend of some Macroeconomic Indicators for OLS Estimation Method (Collectively)

Units of Measurement	In cr.	In cr.	In cr.	In cr.	In cr.	In cr.	In cr.
Year	**FDI**	**GNI**	**PCI**	**RES**	**GCF**	**GDP**	**REER**
2005-06	8,961	3518348	28639	676387	1266073	3543244	102.38
2006-07	2,283	3841974	30805	868222	1540583	3871489	100.76
2007-08	3,484	4233768	33446	1237965	1896799	4250947	109.2
2008-09	4,187	4390966	33987	1283865	2000103	4416350	99.65
2009-10	3,775	4763090	36249	1259665	2351255	4790847	103.88
2010-11	3,485	5227739	39270	1361013	2843415	5282386	112.68
2011-12	4,656	8659505	63462	1506139	3458749	8736329	110.27
2012-13	3,430	9104662	65538	1588418	3813272	9213017	105.57
2013-14	3,605	9679027	68572	1828375	3822003	9801370	103.27
2014-15	4,515	10402987	72805	2137647	4272496	10527674	108.96
2015-16	5,556	11234571	77659	2378740	4423075	11369493	112.09
2016-17	6,022	12153754	82931	2398193	4641287	12298327	114.52
2017-18	6,097	13034121	87623	2597569	5289409	13179857	119.71

***Source**- Economic Survey of India, 2018-19 Statistical Index & FDI Fact Sheet*

In terms of percentage, it can be seen that highest fall in FDI can be seen in the year 2006-07 amounting to (75%) after which there was a sharp increase in the FDI to 53% in 2007-08. As, US Housing Market caused a world economy depression, thus GNI, PCI, GDP and REER all face a steep fall in the year 2008-09 with the percentage of 3.713, 1.618, 3.891 and (8.745) respectively. RES growth was least in the year 2009-10 with (1.885%). GCF also fell in the year 2008-09 but still it was least in the year 2013-14.

Table 5- Trend of some Macroeconomic Indicators for OLS Estimation Method (Collectively) (In Percntage)

Year	FDI	GNI	PCI	RES	GCF	GDP	REER
2005-06	48	9.271	7.548	9.250	20.323	9.285	2.329
2006-07	-75	9.198	7.563	28.362	21.682	9.264	-1.582
2007-08	53	10.198	8.573	42.586	23.122	9.801	8.376
2008-09	20	3.713	1.618	3.708	5.446	3.891	-8.745
2009-10	-10	8.475	6.655	-1.885	17.557	8.480	4.245
2010-11	-8	9.755	8.334	8.047	20.932	10.260	8.471
2011-12	34	65.645	61.604	10.663	21.641	65.386	-2.139
2012-13	-26	5.141	3.271	5.463	10.250	5.456	-4.262
2013-14	5	6.308	4.629	15.107	0.229	6.386	-2.179
2014-15	25	7.480	6.173	16.915	11.787	7.410	5.5098
2015-16	23	7.994	6.667	11.278	3.524	7.996	2.873
2016-17	8	8.182	6.789	0.818	4.933	8.170	2.168
2017-18	1	7.244	5.658	8.314	13.964	7.1679	4.532

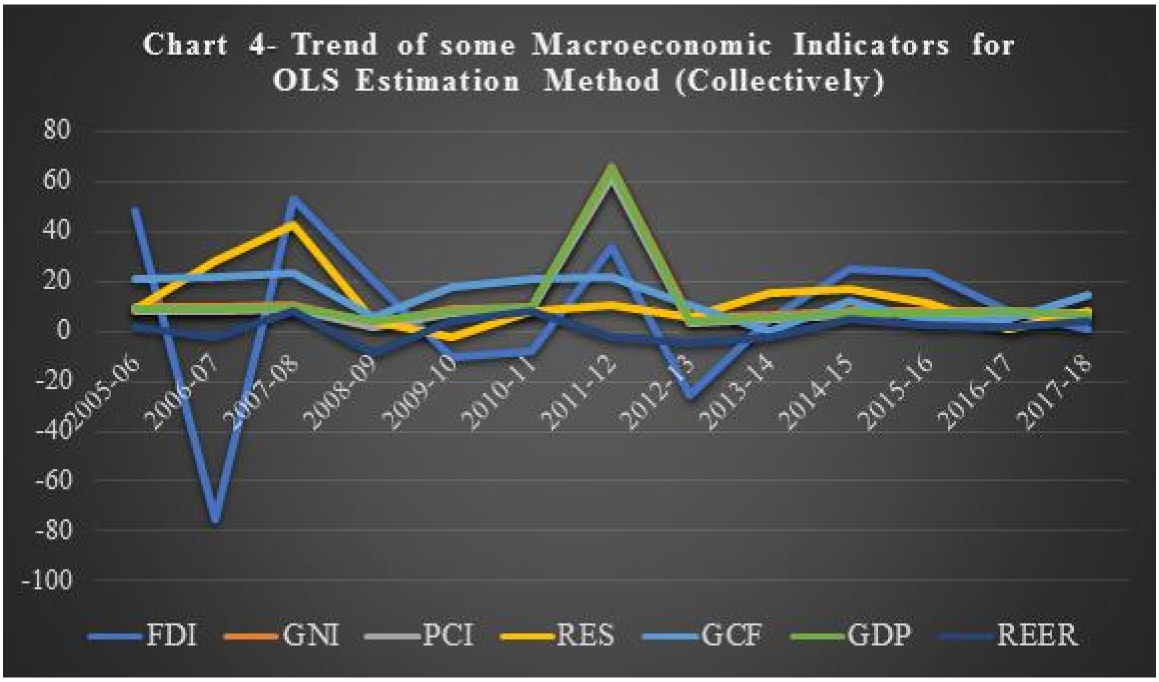
Source- *Computed by author in excel from the data collected*

Note-

1. *The data is rounded off up to 3 decimal places but the OLS Estimation Method is done on non- rounded data.*
2. *Calculation is done by following formula-*

Percentage of the Year 1= [(Data of Year 1-Data of Year 0)/ Data of Year 0] X 100

FDI shows highest growth in the year 2005-06 which is 48%. GNI, PCI and GDP all show highest growth in the year 2011-12 after the effect of depression in the economy is stalled. RES and GCF was highest in 2007-08 with 42.586% and 23.122% respectively just before the crash of the economy. REER saw highest growth in the year 2010-11.



OLS Estimation Equation of the Data-

OLS Estimation equation to study the impact of FDI on Indian economy is as follows-

FDI= a+ b1*GNI+ b2*PCI+ b3*RES+ b4*GCF+ b5*GDP +b6*REER

Where,

a= intercept

b1, b2, b3, b4, b5 and b6= OLS Estimation Coefficients of respective independent variable

FDI= Percentage growth in FDI Equity Inflows

GNI= Percentage growth in Gross National Income

PCI= Percentage growth in Per Capita Income

RES= Percentage growth in Foreign Exchange Reserves

GCF= Percentage growth in Gross Capital FormationGDP= Percentage growth in Gross Domestic Product

REER= Percentage growth in Real Exchange Rate

As per the OLS Estimation model, It can be concluded that GNI, RES and REER ave a positive relationship with FDI with a OLS Estimation coefficient as 131.50, 0.165 and 6.902 while PCI, GCF and GDP has a negative relationship with a OLS Estimation coefficient as (-85.493). (2.673) and (48.462) respectively. Intercept of the equation is negative (92.085) which means if all the indicators are *zero* then value of FDI will be (92.085).

Table 6- Multiple OLS Estimation Coefficients and Probabilities of Some Macroeconomic Indicators				
Variable	**Coefficient**	**Std. Error**	**t-Statistic**	**Prob.**
C	-92.08479058	99.42515883	-0.926171923	0.390089773
GNI	131.4959699	75.84392245	1.733770692	0.133656468
PCI	-85.49375077	72.07362175	-1.186200287	0.280381337
RES	0.165123073	1.196749906	0.137976257	0.894773223
GCF	-2.673239701	2.104182104	-1.27044123	0.250965327
GDP	-48.46224404	62.83027825	-0.771319902	0.469793652
REER	6.902499604	4.641594449	1.48709666	0.187547627
Source- *Computed by Microsoft Excel*				

F-test

F-test is the test to study whether our OLS Estimation model is significant or not. Probability of F-Statistic is the guiding factor to decide whether null hypotheses is accepted or alternate is accepted. The null and alternate hypotheses of the F-test are-

- H_0: $\beta_1 = \beta_2 = ... = \beta_{p-1} = 0$
- H_1: β_j “‘ 0, for at least one value of j

Since Probability- value of F-Statistic is 0.512676995 which is more than 5% confidence level, thus we fail to reject the null hypotheses and accept the alternate hypotheses. The null hypotheses of the study is – FDI has no impact on Indian Economy. As, the null hypotheses is accepted thus it can be concluded that ***FDI has no impact on Indian Economy***, i.e., that F*-test is not significant.*

R-square is the square of correlation of the OLS Estimation model, it indicates the variation in the dependent variable due to change in independent variable. Higher the amount of R-square the better as it is the coefficient of determination. In our OLS Estimation model, *R-square* is *0.493238112*. Thus, it can be said that independent variable defines FDI by 49.33% which is a not bad that our model is not spurious.

The final OLS Estimation equation of the macroeconomic indicators is-

FDI=-92.08479058+131.4959699*GNI+ (85.49375077)*PCI+ 0.165123073*RES+ (2.673239701)*GCF+ (48.46224404)*GDP+ 6.902499604*REER

Table 7- Multiple OLS Estimation Test Results of Some Macroeconomic Indicators	
R-squared	0.493238112
S.E. of regression	33.81078398
F-statistic	0.973313351
Prob(F-statistic)	0.512676995
Source- *Computed by Microsoft Excel*	

KEY FINDINGS AND SUGGESTIONS

The major findings of the article are-

- FDI keeps on fluctuating sometimes at increasing rate sometimes at diminishing rate depending upon the economic condition of the country and world. It implies that as a matter of policy, the host country can depend on regular inflow of FDI if it creates a conducive climate for the purpose.
- According to the data it is observed that there has been significant amount of increase in the amount of FDI Inflow from 2013-14 to 2016-17 in all industries except Real Estate and trading industry. It is sluggish since 2015-16 as there has been no FDI inflow in the industry while Communication Service sector is extremely befitted from FDI.
- It can be concluded from the above discussion that FDI in India is majorly contributed by Mauritius and Singapore in absolute terms but in comparison to increase in the amount of percentage as compare to earlier years the major contributor is Cayman Islands and Canada. Japan and Cyprus are among the two major countries which observed decrease in the amount of FDI in India both in absolute and percentage terms.
- There is no impact of Total FDI Inflows on Indian Economy as the ANOVA Test fails to be significant.

The key suggestions from the above discussion are-

- The government need to have a robust and compatible FDI Policy to reap the benefits of FDI.
- There is an emergent need to make India an attractive destination for FDI., government need to have more promotion and better infrastructure facilities to increase the FDI Inflow in India.
- There is a need to strengthen our Education sector, so that we can provide much skilled labor. More schools, infrastructure is needed to boost FDI Inflow in India.

CONCLUSION

From the above discussion, it can be concluded that even though amount of FDI Inflow have increased since the implementation of LPG Policy still FDI do not have impact on Indian Economy. The data reveals some sector being benefitted from FDI and some are not but in broader frame FDI have no Impact on Indian Economy. The better analysis could be done with a detailed analysis of sector or industry in which FDI invest their money.

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