A STUDY OF FDI TRENDS AND INDIAN ECONOMY

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ABSTRACT

FDI has been one of the most influential forces in boosting the growth rate of Indian economy. It has been viewed as a bundle of supplies including capital, technology, skills and sometimes even market access.FDI helps in transferring of financial resources, technology and innovative and improved management techniques along with raising productivity. This study examines the trend of FDI inflows in India. For the present study the trend analysis with 4 yearly moving averages is the primary statistical tool employed. The empirical results show that a FDI inflow leads to increasing trend in the economic growth of the country and has the positive impact on the economy.

Keywords: Foreign Direct Investment, Inflation, Gross Domestic Product, Spillover, Trade Openness, Foreign Exchange Reserves

FOREIGN DIRECT INVESTMENT

Foreign direct investment (FDI) is an integral part of an open and effective international economic system and a major catalyst to development. FDI has become an increasingly more important factor of economic growth. India opened its doors for the FDI inflow in the year 1991 with the Government’s liberalization and economic reforms programme which aimed at rapid and substantial economic growth and integration with the global economy in a harmonized manner. The industrial policy reforms reduced the industrial licensing requirements, removed restrictions on investment and expansion, and facilitated easy access to foreign technology and foreign direct investment.

FDI can be described in simple language an investment done by a foreign company or individual in productive growth of another nation.FDI is a capital exchange between national borders that gives the sense of control to the investors over the gained assets. As International Monetary Fund quotes it, FDI is an "investment that is made to acquire a lasting interest in an enterprise operating in an economy operating other than that of investor". UNCTAD definition WIR 02 has defined FDI as "an investment involving long term relationship and reflecting a lasting interest and control by a resident entity in one economy (foreign direct investor or parent enterprise) in an enterprise resident in an economy other than that of the FDI enterprise, affiliate enterprises or foreign affiliate. FDI is the process in which the residents of source country acquire the ownership of assets for the purpose of controlling the production, distribution and other productive activities of a firm in the host country. FDI is a direct investment which is different from indirect investment such as portfolios inflows, acquisition of stock of an enterprise, bonds and debentures etc.

AN OVER VIEW OF FDI IN INDIA

The historical background of FDI in India can be traced back with the establishment of East India Company of Britain. British capital came to India during the colonial era of Britain in India. After Second World War, Japanese companies entered Indian market and enhanced their trade with India, yet U.K. remained the most dominant investor in India. Further, after Independence issues relating to foreign capital, operations of MNCs, gained attention of the policy makers. Keeping in mind the national interests the policy makers designed the FDI policy which aims FDI as a medium for acquiring advanced technology and to mobilize foreign exchange resources. With time and as per economic and political regimes there have been changes in the FDI policy too. The industrial policy of 1965, allowed MNCs to venture through technical collaboration in India. Therefore, the government adopted a liberal attitude by allowing more frequent equity participation to foreign enterprises, and to accept equity capital in technical collaborations. But due to significant outflow of foreign reserves in the form of remittances of dividends, profits, royalties etc, and the government has to adopt stringent foreign policy in 1970s. During this period the government adopted a selective and highly restrictive foreign policy as far as foreign capital, type of FDI and ownerships of foreign companies was concerned. Government setup Foreign Investment Board and enacted Foreign Exchange Regulation Act in order to regulate flow of foreign capital and FDI flow to India. The soaring oil prices continued low exports and deterioration in Balance of Payment position during 1980s forced the government to make necessary changes in the foreign policy. The government introduced reforms in the industrial sector, aimed at increasing competency, efficiency and growth in industry through a stable, pragmatic and non-discriminatory policy for FDI flow. In this critical face of Indian economy the government of India with the help of World Bank and IMF introduced the macro – economic stabilization and structural adjustment program. As a result of these reforms India open its door to FDI inflows and adopted a more liberal foreign policy in order to restore the confidence of foreign investors. Further, under the new foreign investment policy Government of India constituted FIPB (Foreign Investment Promotion Board) whose main function was to invite and facilitate foreign investment through single window system from the Prime Minister's Office. The foreign equity cap was raised to 51 percent for the existing companies. Government had allowed the use of foreign brand names for domestically produced products which was restricted earlier.

ROUTES FOR INWARD FLOWS OF FOREIGN DIRECT INVESTMENT

Foreign Direct Investment (FDI) into India is allowed through two channels:-

a.) Automatic Route: FDI under automatic route does not require prior approval either by the Govt. of India or the Reserve Bank of India (RBI). Investors are only required to notify the concerned Regional office of RBI within 30 days of receipt of Inward remittances and file required documents with that office within 30 days of issue of shares to foreign investors**.** The automatic approval route of the RBI was introduced to facilitate FDI inflows. However, during post-policy period, the actual investment flows through the automatic route of the RBI against total FDI flows remained rather insignificant. This was partly due to the fact that crucial areas like electronics, services and minerals were left out of the automatic approval route. Another limitation was the ceiling of 51 per cent on foreign equity holding. An increasing number of proposals were cleared through the FIPB route while the automatic approval route was relatively unimportant. However, since 2000 automatic approval route has become significant and accounts for a large part of FDI inflows.

b.) Government Approval Route : For the following categories, Government approval for FDI through the Foreign Investment Promotion Board (FIPB) is necessary:-

i.) Proposals attracting compulsory licensing

ii.) Acquisition of existing shares.

FIPB ensures a single-window approval for the investment and acts as a screening agency. FIPB approvals are normally received in 30 days. RBI introduced automatic approval system in 1992 to facilitate more convenient entry to foreign investors. From 1996, FDI inflows on acquisition of shares have also been included and have been rising continuously since 2004 whereas FDI Inflows through NRI's route have been declining especially since 2002.

DETERMINANTS OF FOREIGN DIRECT INVESTMENT (FDI) IN INDIA

In the present section, the major factors which have determined the inflows of FDI in India in the Post-Reform period are discussed. A country which has a stable macroeconomic condition with high and sustained growth rates will receive more FDI inflows than a more volatile economy. The variable that measures the economic stability and growth are Gross Domestic Product (GDP), inflation rates, Trade Openness and Foreign exchange reserves. Investors prefer to invest in more stable economies that reflect a lesser degree of uncertainty and risk. Market size also plays an important role in attracting Foreign Direct Investment (FDI) from abroad and it is measured by GDP. Market size tend to influence the inflows, as an increased customer base signifies more opportunities of being successful and also the fact that with the rampant development the purchasing power of the people has also been greatly influenced moving to many levels higher in comparison to what it was before the economic growth. Trade openness is also considered to be one of the key determinants of FDI as represented in the past literature; much of FDI is export oriented and may also require the import of complementary, intermediate and capital goods. Thus, trade openness is generally expected to be a positive and significant determinant of Foreign Direct Investment (FDI).

THEORTICAL BACKGROUND

This section reviews the empirical studies on the FDI in India and sectoral analysis which could study the positive impact of FDI on growth of the countries and the flows of FDI in sectors in regards to GDP. Laura Alfaro (2003) in the paper ‘foreign direct investment & growth’ stated that although it may seem natural to argue that foreign direct investment (FDI) can convey great advantages to host countries, the benefits of FDI vary greatly across sectors. The foreign direct investment effects on growth in the primary, manufacturing, and services sectors. Kulwindar Singh (2005) stated in paper that the government while serious in its efforts to induce growth in the economy and country started with foreign investment in a haphazard manner. While it is accepted that the government was under compulsion to liberalize cautiously, the understanding of foreign investment was lacking. Blomstrom and kokko (2003), they said in their paper that least developed economies attracting less FDI. It suggests that the existence of threshold level of development is necessary for FDI. Having more attraction of FDI inflows in least developed economies that results in boosting the economy of a country. Dr Maathai K. Mathiyazhagan (2005), This paper studied the annual period data from 1990-91 to 2000-01 as to examine the long run relationship of FDI with Gross Output, Export and Labour Productivity at sectoral level in the Indian Economy. FDI Inflows into the sectors is to boost the output, labour productivity and export in some sectors and it is to be tested by the panel co-integration (PCONT) test. This results as that there is no significant cointegration and hence, concluded that FDI has not able to hold a positive impact at the sectoral level on the Indian economy. And the whole study suggests that to expand export oriented sectors and the higher growth of the economy could be achieved through the growth of these sectors. Bose, Jayashree (2007), the book studied the sectoral analysis of India & China related to FDI Inflows. In his book, he lights on the emerging issues on FDI inflows in India & China comparatively and also on the globalization, foreign factors, trends & issues on FDI outflow from India and China. Khan A.Q. and Siddiqui Ahmad Taufeeque (2011), studied the impact of FDI on Indian economy and a comparison with China & USA. The paper has also been ventured into carving out set of strategies to deal with the issues & problems in attracting FDI for promotion & growth of international trade. The double log model has been used to find elasticity between different factors in this paper. They also highlight the impact of FDI on employment. In this research paper, the discussion between FDI and GDP as to asses that FDI helps in boosting growth of a country. Bhanagade D.B, Shah A. Pallavi (2011), they said in their paper that the impact of FDI on Indian Economy where they also emphasize on the investments, sectors attracting highest FDI inflows and FDI leads to Generation of Employment opportunities. Therefore the growth of inflow of FDI would lead to positive growth of Gross capital formation. In India, the growth of GDP is largely influenced by FDI. Chaturvedi Ila (2011), In this paper, analyze the FDI inflows with special reference to sector wise inflows in India. This paper also explore the sector wise distribution of FDI in order to know the dominating sector which has attracted the major share of FDI in India. And to find out the correlation between FDI and Economic Development, It reveals that there is high degree of significance between FDI and economic development. Vohra and Sehgal did an evaluation in 2011 approximately trends and styles of foreign funding in India and to recognize about the worldwide state of affairs and to study the relationship of liberalised regime pursued by the international locations with the extent of FDI inventory. Regression analysis was executed among FDI Restrictiveness Index (FDI Index) and degree of FDI stock to provisionally check this relationship. The outcomes exhibited a compelling courting between this index and the extent of FDI stock, sincerely implying that if economy is extra open with much less of regulations the inflow of FDI may be greater and vice-versa. Similar analysis was done by Hooda Sapna in 2011 regarding the impact of FDI on the economic growth of Indian economy for the period 1991-92 to 2008-09. She observed that the FDI plays the important role in the growth of the economy by using the OLS method. It was also found that trade GDP, research and development GDP, financial position, exchange rate, Foreign exchange reserves GDP were the important macroeconomic determinants of FDI Inflows in India. Comparable analysis becomes performed via Hooda Sapna in 2011 regarding the impact of FDI at the financial growth of Indian financial system for the period 1991-92 to 2008-09. She determined that the FDI performs the essential position inside the boom of the economy by the use of the OLS technique. It turned into also observed that change GDP, studies and development GDP, monetary role, alternate charge, foreign exchange reserves GDP had been the crucial macroeconomic determinants of FDI Inflows in India. Samal Sanghamitra , Raju D.Venkatrama (2016) research the float of FDI into production quarter in India & its effect for manufacturing increase in Indian Industries for enhancing the monetary boom in line with capital in addition to the domestic region. The present study attempts to assess the determinants and impact of FDI in Indian financial elements. For this reason, the present look at is an endeavour to talk about the trends and styles of FDI, and its effect of FDI on Indian economy. This paper analysed FDI inflows from 2000 to 2014 into manufacturing sectors. Hooda Shailender (2016) examines the repute of and tendencies in overseas funding influx into the Indian health centre area and highlights the rising troubles from 2000 to 2014, the technology of liberalised overseas investment. At some stage in this period a widespread number of firm players focussed on the Indian hospital quarter—increasing their presence via partnerships and investments in joint task initiatives. although foreign funding inflow to hospitals elevated hundredfold for the duration of the period, an exam of decided on main company hospitals of India, but, displays that global investments represent a small percentage within overall financing; alternatively, it's miles the lengthy-time period domestic borrowing that dominates. normal, overseas investments has largely been utilized in awesome-speciality and tertiary cares offerings, especially in metropolitan cities, even as investment for primary and secondary cares, clinical research, drug development, diagnostic services for rural region remained negligible. The look at argues that personal funding can play a complementary function in offering tertiary and speciality care services, specially inside the untapped hospital marketplace, and it need to now not be taken into consideration instead for public provisioning of healthcare services. The authorities ought to growth its healthcare spending manifold so that it will offer price-powerful care to the overall population across the -, along with within the remotest areas.

OBJECTIVES OF THE STUDY

The study covers the following objectives:

- To examine the trends of the foreign direct investments in India
- To Forecast the FDI inflows in the Economy for next 5 years.

NATURE AND SOURCE OF DATA

The present study is of analytical nature and makes use of secondary data. It is a time series data. The relevant secondary data has been collected from reports of the Ministry of Commerce and Industry, Department of Industrial Promotion and Policy, Government of India, Centre for Monitoring Indian Economy, Reserve Bank of India and World Investment Report

RESEARCH METHODOLOGY

- **TREND ANALYSIS**

  $\hat{y} = a + b\,x$

where

$\hat{y}$ = predicted value of the dependent variable

a = y – axis intercept,

b = slope of the regression line (or the rate of change in y for a given change in x),

x = independent variable (which is *time* in this case).

On the basis of the terend analysis the trend line is drawn and shown in the fig no 4.2

- **COMPOUND ANNUAL GROWTH RATE**

Compound Annual Growth Rate is worked out by using the following formula:

CAGR (t0, tn) = (V(tn)/V(t0))1/tn – t0 -1 where

$V(t0)$: start value, $V(tn)$: finish value, $tn - t0$: number of years.

In order to analyse the collected data, various statistical and mathematical tools were used.

- **FORECASTING**

The forecast formula calculates the base forecast for the next period as the average of historic base demand for a specified number of periods. This is denoted in the following equation:

$$F(i + 1) = (D(i) + D(i - 1) + ... + D(i - (n - 1))) / n$$

The number of periods used determines how quickly the averaging will react to changes in actual trends and how sensitive it will be to random variations. The more periods included will make the calculation method more stable from random variations, but it will also react more slowly to changes resulting from real trends.

RESULTS AND DISCUSSIONS

TREND ANAYSIS

The data of FDI inflows have been recorded from pre liberalisation period i.e 1980 onwards till date The data and its graphical presentation of the data depicts that FDI inflows was very low but were in increasing mode and has the positive impact on the economic growth of the economy. The major changes has been observed in the year 2007-08 and after that it increased exponentially along with decline at few times .The moving average has been calculated on 4 year basis from 1980 onwards table no 1.1 and its graphical presentation is shown on Fig no 1.1 and 1.2 .

Table 1.1 FDI Inflows in India

Years	FDI Inflow (US million $)	Moving Average
1980-81	8	
1981-82	10	
1982-83	60	
1983-84	60	34.5
1984-85	60	47.5
1985-86	160	85

1986-87	196	119
1987-88	190	151.5
1988-89	267	203.25
1989-90	330	245.75
1990-91	97	221
1991-92	129	205.75
1992-93	315	217.75
1993-94	586	281.75
1994-95	1314	586
1995-96	2144	1089.75
1996-97	2821	1716.25
1997-98	3557	2459
1998-99	2462	2746
1999-2000	2155	2748.75
2000-01	4029	3050.75
2001-02	6130	3694
2002-03	5035	4337.25
2003-04	4322	4879
2004-05	6051	5384.5
2005-06	8961	6092.25
2006-07	22826	10540
2007-08	34835	18168.25
2008-09	41874	27124
2009-10	37745	34320
2010-11	34847	37325.25
2011-12	46556	40255.5
2012-13	34,298	38361.5
2013-14	36,046	37936.75
2014-15	45,148	40512
2015-16	55,559	42762.75
2016-17	60,082	49208.75
2017-18	61963	55688

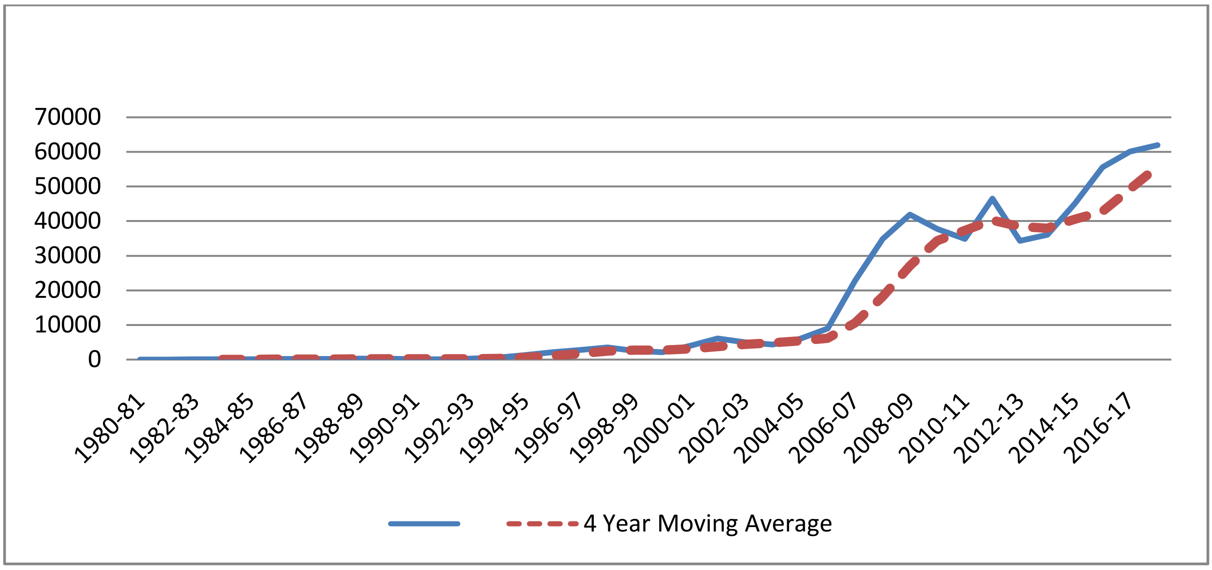

Fig 1.1 FDI Inflows in India

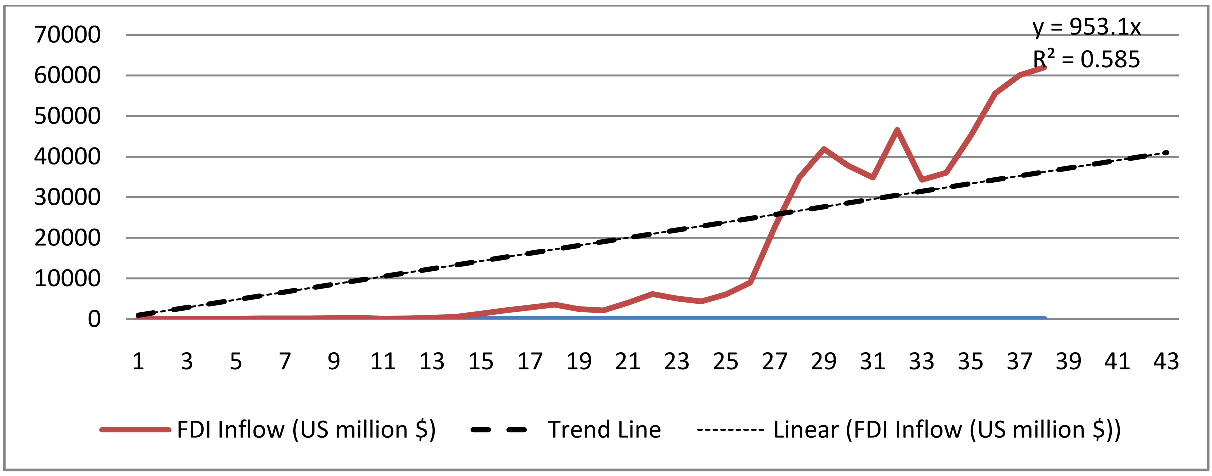

Fig 1.2 FDI Inflows in India showing the trend line as well as forecasted FDI inflows for next 5 years

The forecasting values for the next 5 years which is depicted through the dotted line in fig no 1.2 :

35002.5

35900

36797.5

37695

38592.5

The CAGR value is 0.490745182

CONCLUSIONS

It is strongly believed that it is in India's interest to continue to boost foreign investment by Liberalizing rules on equity caps, investment reviews and other provisions that have impeded India's ability to attract even more foreign investment over the recent years.. There has been a generous flow of FDI in India since 1991 and its overall direction remained the same over the years irrespective of the ruling party. A comparative analysis of FDI approvals and inflows reveals that there is a huge gap between the FDI amount approvals and inflows reveals that there is a huge gap between the amount of FDI approved and its realization into actual disbursements in India. **FDI** is considered to be the life blood and an important vehicle of for economic development as far as the developing nations are concerned. The important effect of FDI is its contribution to the growth of the economy. FDI has an important impact on country's trade balance, increasing labour standards and skills, transfer of technology and innovative ideas, skills and the general business climate. FDI also provides opportunity for technological transfer and up gradation, access to global managerial skills and practices, optimal utilization of human capabilities and natural resources, making industry internationally competitive, opening up export markets, aceess to international quality goods and services and augmenting employment opportunities.

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