Foreign Direct Investment in Trends in India in the New Millennium

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Abstract

Global foreign direct investments serve as an attractive source of funding for infrastructure development and economic growth of nations. It is more significant for emerging economies like India, China and Brazil. Economic reforms initiated in various countries facilitate the integration of various economies into the global trading platform. This in turn helps in the foreign direct investment inflows into various countries. In this research paper, an attempt is made to understand the foreign direct investment inflows into India in the new millennium. The analysis presented in this research focuses on the time period April 2000 – March 2016. The results of the study indicate that India has experienced a steady increase in FDI inflows.

Key Words:

Economic reforms; Equity inflows; foreign direct investment inflows; India

Introduction

Foreign direct investment (FDI) is considered to be one of the channels of economic growth for any economy. Internal and external investments were of prime concern to many emerging economies in the world (Azhar & Marimuthu, 2012). Indian economy is no exception to this phenomenon. India embraced globalization in 1991 and initiated a number of economic reforms aimed at strengthening the Indian economy. During the last 25 years of India's economic reforms period, India has witnessed an increasing trend in FDI. FDI inflow into any country complements the domestic investments which facilitates economic growth, technological up-gradation and enhancement of managerial skills.

Many researchers have investigated the determinants of FDI into various economies in the world (Angelo et, al. 2010; Kaur et, al. 2013; Maniam & Chatterjee, 1998; Singhania & Gupta, 2011). Empirical evidence suggests that many factors influence the FDI inflow into any host country. The main factors include the size of the host country market, resource endowments, infrastructure facilities, macroeconomic stability, political stability and transparent policy framework to attract FDI (Balasubramanyam & Mahambare, 2003). Prior research indicates that capital inflows in the form of FDI are beneficial for economic development (Vishwakarma, 2015).

In this back drop, India had opened up its economy in 1991 to integrate its trade with the global markets. This has resulted in a continuous inflow of FDI into Indian economy for the past 25 years. This research attempts to capture the trends in the FDI inflows into Indian economy in the 21st century focusing on the period April 2000 – March 2016. This research is structured as follows: after the introduction section, a review of literature is presented. This is followed by objectives of the study and the research methodology. Subsequently, analysis of the data was presented. Finally the research paper presents a conclusion regarding the trends of FDI inflows into India.

Review of Literature

Angelo et al (2010) investigated the relative importance of various factors that exhibited a significant impact on the flow of foreign direct investment (FDI) into Brazil. The study employed two-stage least squares regression approach to identify the determinants of FDI into Brazil during the period 2000-2007. Aggregate retail sales in Brazil, exchange rate, interest rate for consumer financing and attractiveness of the Brazilian market were considered as the independent variables that have an impact on flow of FDI into Brazil. The results indicated that aggregate retail sales were a significant determinant of FDI inflow into Brazil. Interest rate was found to have a negative influence on the flow of FDI. Exchange rate was also found to have a significant impact on FDI inflow into Brazil but was found to be less significant in comparison to aggregate retail sales. Finally, no evidence was found to suggest the impact of attractiveness of Brazilian market on the flow of FDI into the country.

Azhar and Marimuthu (2012) presented an analysis of FDI inflow into India during the period 2000-2010. The authors highlighted that stable economic policies, economic factors, cheap and skilled labour, basic infrastructure, unexplored markets and availability of natural resources are the key determinants of FDI into India. The research methodology used in the study was descriptive in nature employing the data available from the Department of Industrial Policy and Promotion (DIPP). The authors have provided a summary of year-wise FDI inflow into India during 2000-2010. Additionally, sectoral-wise FDI inflow into India was also analysed. The results indicated that Electrical equipments industry attracted the highest FDI inflow with nearly 15.6 per cent of total FDI inflow into India.

Balasubramanyam and Mahambare (2002) examined the phenomenon of FDI inflow into India in the context of India's economic reforms that were initiated in 1991. The authors concluded that FDI is a significant channel for transfer of technology and know-how into developing countries like India. It was also observed that the FDI inflow into India has increased significantly after the economic reforms and had a positive impact on the growth, exports and productive efficiency of the Indian industry. The study includes an analysis of FDI inflow into India in terms of foreign collaborations and sectoral-contribution including a state-wise analysis of FDI inflow into India.

Buckley et al (2012) analysed the FDI inflow of Japanese multinational firms into Indian economy using an institutional approach. The authors highlighted the Japanese firms have a long history of engaging in outward FDI as a stimulus for the economic growth of Japan. The sectoral analysis indicated that specific industries like electronics and automotives have had a strong impact of FDI inflow into India.

Collins et al (2008) investigated the relation between home country institutional frameworks as predictors of FDI into India. A sample of 51 countries that invested in India during the period 1996-2000 was considered for the study. Approved FDI transactions and actual FDI transactions were considered as the dependent variables. Overall institutional environment, regulative environment, cognitive environment and normative environment were considered as independent variables. GDP, labor cost, inflation rate and bilateral treaties were considered as control variables. The results indicated that home country institutional frameworks had a significant impact on FDI inflow into India. Regulative environment and cognitive environment were also found to have a positive impact on FDI into India while normative environment was not observed to be a predictor of FDI into India.

Deshmukh (2011) analysed the FDI patterns in India during the post-economic reforms period after 1991. The study revealed that FDI into India increased sharply after the economic reforms were initiated. The author concluded that FDI can complement local development by increasing export competitiveness, employment generation, strengthening of local skills and increased financial resources for economic development. The research also highlighted the major countries which had been the historical sources of FDI into India.

Dharmaraj and Kathirvel (2013) investigated the financial performance of Indian automobile industry during the pre and post FDI inflows into India. 48 Indian automobile firms were included in the study for the period 1999-2012 using CMIE Prowess database. Various financial ratios were examined to investigate the financial performance of the sample firms during the period of study. The ratios considered were – current ratio; quick ratio; inventory to total assets ratio; quick assets to total assets ratio; current assets to total assets ratio and working capital to total assets ratio. Return on sales, return on equity, return on total assets, return on capital employed, operating profit to sales ratio and net income to total debts ratio were considered to analyse financial performance of the automobile firms. Inventory turnover ratio, debtors turnover ratio, fixed assets turnover ratio and working capital turnover ratios were calculated to estimate the efficiency of the firms. Total debt to total assets ratio, net fixed assets to equity ratio, debt-equity ratio and long term debt-equity ratio were analysed to understand the long term solvency position of the Indian automobile firms. The authors concluded that there is a significant impact of FDI on the liquidity of Indian automobile industry. The analysis of profitability ratios concluded that the profitability of Indian automobile industry has exhibited an increase in the post reforms period.

Kaur et al (2013) investigated for a causal relationship between FDI into India and the economic growth of the country. Gross Domestic Product (GDP) was considered as the proxy for economic growth. The results of the study concluded that GDP and FDI were integrated in the long run during pre-economic reforms and post-economic reforms in India.

Maniam and Chatterjee (1998) have examined the determinants of USA's FDI in India during the period 1962 – 1994. Multiple regression analyses was carried out to arrive at the conclusions of the research. The independent variables considered in the research were gross national product; growth of the market size, trade balance, exchange rate. Ratio of US FDI to host country's real GNP was considered as the dependent variable. Exchange rate was found to have a significant and positive impact as a determinant of USA's FDI into India.

Mora and Singh (2013) explored the relationships between the nature of exports and imports for growth and the relevance of FDI for trade productivity and trade fragmentation in the context of Asian economies. The authors concluded that FDI is positively correlated with higher productivity levels in exports and imports for many countries in the sample. China, Hong Kong, India, Indonesia, Japan, Korea, Malaysia, Singapore, Taiwan and Thailand were included in the sample of Asian economies.

Nandi and Sahu (2007) analysed the FDI inflow into Indian retail market. The authors highlight that FDI is really important for the Indian economy as a whole and for the retail sector in particular. The authors also argue that FDI in retail trade should be allowed and the extent of FDI should not be limited.

Pradhan et al (2004) evaluated the impact of employment and wage effects of FDI in Indian manufacturing sector. The findings of the study conclude that foreign companies do not have any negative impact on employment levels in Indian manufacturing industries as compared to the domestic firms. It was observed that foreign firms tend to pay relatively higher wages to employees in comparison to their Indian counter parts. The research highlights that the labour market in India had benefited from FDI inflow into India.

Prusty and Vishwakarma (2014) examined the relation between FDI inflow into India and GDP of Indian economy in the post-liberalisation period by making a comparison with the pre-liberalisation period. The study concluded that FDI is a significant factor that has an impact on the GDP of Indian economy. Data for the study included the period during 1981 – 2013. The findings of the study indicate the FDI inflow into India was much stronger in the post-liberalisation period. Singh and Paul (2014) investigated the FDI inflow into India during the period 1990-2012. GDP, outward FDI and export were found to have a significant impact on FDI inflow into India while imports were not found to be significant determinants of FDI inflow.

Singhania and Gupta (2011) examined the various determinants of FDI into India using various macro economic variables. GDP, inflation rate, interest rate, patents, money growth and foreign trade were employed as independent variables. GDP, inflation rate and scientific research (patents) were found to have a significant impact on FDI inflow into India. The period of the research was during 1995-1997.

Tripathi et al (2015) studied the link between macro economic factors and FDI inflow into India. Exchange rate, inflation, GDP, interest rate, trade openness and profitability index were considered as independent variables. All the variables except exchange rate were found to have a significant impact on FDI inflows into India.

Vishwakarma (2015) analysed the relation between FDI into India and its economic growth after economic liberalisation. The period of the research was during 1991-2013. GDP was considered as a proxy for FDI inflow into India. The analysis concluded that there is a strong link between FDI into India and its GDP.

It can be observed that many of earlier studies have not captured the latest trends regarding the FDI inflows into India while some studies investigated the differences in FDI trends in India during pre and post-economic reforms period in India. The analysis of this research paper aims to fill this gap by focusing on the FDI trends in the new millennium.

Objectives and Research Methodology

The objective of this research paper is to understand the trends in FDI inflow into India during the period April 2000 – March 2016. This research is descriptive in nature and draws secondary data from various sources like Department of Industrial Policy and Promotion (DIPP), Ministry of Commerce and Industry, Government of India; United Nations Conference on Trade and Development (UNCTAD), World Trade Organisation (WTO). The study focuses on the inflow of FDI into in the new millennium during the period April 2000 – March 2016.

Analysis and Discussion

FDI into India has increased at a rapid paced after economic reforms in India. Table 1 presents a summary of FDI inflows into India during the new millennium (April 2000 – March 2016). It can be observed that the FDI inflow into India has increased from US$ 4.03 billion to US$ 55.46 billion during the period considered for the research registering a compounded annual growth rate (CAGR) of nearly 19.1 per cent. This indicates that the economic reforms in India have enhanced the FDI inflows into India during the period of research. It can also be inferred from Table 1 that India was able to attract nearly US$ 425 billion in the new millennium.

Table 1: FDI Inflows into India during April 2000 – March 2016

Financial Year	US$ (million)	Growth %
2000-2001	4,029	
2001-2002	6,130	52.0
2002-2003	5,035	-18.0
2003-2004	4,322	-14.0
2004-2005	6,051	40.0
2005-2006	8,961	48.0
2006-2007	22,826	155.0
2007-2008	34,843	53.0
2008-2009	41,873	20.0
2009-2010	37,745	-10.0
2010-2011	34,847	-8.0
2011-2012	46,556	34.0
2012-2013	34,298	-26.0
2013-2014	36,046	5.0
2014-2015	45,148	25.0
2015-2016	55,457	23.0
Total	**424, 167**	**19.1 (CAGR)**

Source: Department of Industrial Policy & Promotion (http://dipp.nic.in/English/Publications/FDI_Statistics/2016/FDI_FactSheet_JanuaryFebruaryMarch2016.pdf)

Further anlaysis regarding the source of FDI inflows into India gives interesting insights. It can be observed from Table 2 that India was able to attract FDI from various countries in the world. Mauritius emerged as the country contributing the largest FDI inflow into India. This can be attributed to the tax benefits and the financial system existing in that country which favoured the flow of FDI into India. It is followed by Singapore, United Kingdom, Japan and USA. Interestingly, the top 10 countries that contribute FDI inflows into India account for nearly 60 per cent of total FDI into India. It is expected that similar trends will continue in the near future owing the continuation of economic reforms in India in the near future.

Table 2: FDI Inflows into India – Top 10 Countries

S. No.	Country	Amount of FDI		
		(Rs. crores)	**(US$ million)**	**Growth %**
1	Mauritius	4,80,363.1	95,909.7	33.2
2	Singapore	2,56,666.8	45,879.6	15.9
3	United Kingdom	1,15,591.9	23,108.4	8.0
4	Japan	1,10,671.4	20,966.0	7.3
5	USA	94,574.9	1,7943.4	6.2
6	Netherlands	94,533.1	1,7314.5	6.0
7	Germany	44,870.1	8,629.3	3.0
8	Cyprus	42,680.8	8,552.4	3.0
9	France	26,525.0	5,111.5	1.8
10	UAE	21,648.2	4,029.9	1.4
	Total Top 10 Countries	**1288125.3**	**247444.5**	
	% of Total FDI		**58.3**	

Source: Department of Industrial Policy & Promotion (http://dipp.nic.in/English/Publications/FDI_Statistics/2016/FDI_FactSheet_JanuaryFebruaryMarch2016.pdf)

It is also pertinent to note the trends of FDI inflows into India for various industry sectors in India. Table 3 presents a summary of the 10 ten sectors that attracted the highest FDI inflows in India during the period considered for research.

Table 3: FDI Inflow into India – Top 10 Sectors

S. No.	Sector	Amount of FDI Inflows (April 2000 - March 2016)		% of Total Inflows
		(Rs. crores)	**(US$ million)**	
1	Services	258,354.22	50,792.42	17.6
2	Construction Development	113,936.35	24,187.94	8.38
3	Computer Software & Hardware	112,183.92	21,017.77	7.28
4	Telecommunications	92,728.71	18,382.35	6.37
5	Automobile Industry	81,394.21	15,064.59	5.22
6	Drugs & Pharmaceuticals	70,097.36	13,849.50	4.80
7	Chemicals (excluding fertilizers)	59,555.37	11,900.29	4.12
8	Trading	68,836.54	11,872.47	4.12
9	Power	52,613.34	10,476.15	3.63
10	Hotel & Tourism	49,709.68	9,227.33	3.20
	Total Top 10 Sectors	**959,409.70**	**186,770.81**	**64.72**

Source: Department of Industrial Policy & Promotion (http://dipp.nic.in/English/Publications/FDI_Statistics/2016/FDI_FactSheet_JanuaryFebruaryMarch2016.pdf)

It can be observed that Services industry attracted the maximum FDI followed by construction sector, computer software & hardware, telecommunications and automobile industries. This is in line with the growth of services sector in India which had a positive impact on other sectors like construction, technology, telecommunications and automobile industries. This inflow was facilitated by the enhanced income levels of Indians who have benefited economically due to the globalization process. It can further be observed from Table 3that the top 10 sectors contribute to nearly 65 per cent of all the sectors in the Indian economy indicating the attractiveness of these industries.

Table 4 gives an account of FDI equity inflows into India during the period of research considered for the study. This indicates the investments brought into India by foreign firms. It can be observed from Table 4 that the FDI equity inflows into India increased from US$ 2.46 billion to US$ 40.0 billion with a CAGR of 20.4 per cent in the new millennium. This shows that the global firms have an increasing faith in the strength and future potential of Indian economy.

Table 4: FDI Equity Inflows into India during April 2000 – March 2016

Financial Year	**Amount of FDI Equity Inflows**		**% Growth**
	(Rs. crores)	**(US$ million)**	**(in US$)**
2000-2001	10,733	2,463	
2001-2002	18,654	4,065	65
2002-2003	12,871	2,705	-33
2003-2004	10,064	2,188	-19
2004-2005	14,653	3,219	47
2005-2006	24,584	5,540	72
2006-2007	56,390	12,492	125
2007-2008	98,642	24,575	97
2008-2009	142,829	31,396	28
2009-2010	123,120	25,834	-18
2010-2011	97,320	21,383	-17
2011-2012	165,146	35,121	64
2012-2013	121,907	22,423	-36
2013-2014	147,518	24,299	8
2014-2015	189,107	30,931	27
2015-2016	262,322	40,001	29
Total	**1,495,860**	**288,635**	**20.4 (CAGR)**

Source: Department of Industrial Policy & Promotion (http://dipp.nic.in/English/Publications/FDI_Statistics/2016/FDI_FactSheet_JanuaryFebruaryMarch2016.pdf)

Conclusions

25 years of economic reforms in India that were initiated in 1991 revolutionised the growth of the Indian economy. This had a positive impact on the FDI inflow into India over the last two and half decades. This research focused on the trends of FDI inflow into India in the new millennium during the period April 2000 – March 2016. The analysis indicates that FDI

inflows into India have shown a robust growth over the years. Global economic slowdowns and other external factors did not show a negative impact on the inflow of FDI into India. Though India was successful in attracting a high amount of FDI inflow, it will need to face the challenge of overcoming the attractiveness of China as a global destination for FDI inflows.

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