AN ANALYSIS OF FOREIGN DIRECT INVESTMENT IN INDIA: POST LIBERALIZATION ERA

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ABSTRACT

In the Indian economic situation, FDI is a buzzword. The Indian government has recognised the importance of FDI since the liberalisation of the economy and formulated a selective strategy to attract FDI. The strategy has many goals, such as self-reliance, the security of national industries and entrepreneurs, the importation of selected technologies and the promotion of exports. It has become more important than trade to boost international economic transactions. Performance, technological growth, and infrastructure strengthening and job creation opportunities are encouraged by non-debt-generating capital inflows from foreign investors. Thus, each economy seeks to attract FDI by creating a favourable environment for foreign investment and by providing facilities and incentives for foreign investors. An attempt has been made in this paper to examine the FDI patterns over the past three decades, i.e. from 1991-2019. The relationship between FDI and the capital account is also studied.

Keywords: *Foreign Direct Investment (FDI), Capital Account, Trends, Liberalisation, Economic Development.*

Introduction

The FDI's position in the cycle of economic growth has been a hot topic of discussion in several countries including India. FDI is a crucial part of the world economy's attempts to globalize. International manufacturing development is driven by economic and technological forces. It is also driven by the ongoing liberalization of FDI, and trade policies. The circulation of private capital flows in the form of foreign direct investment (FDI) in developing countries has been an outstanding feature of the world today, especially since the 1990s. FDI flows include capital provided directly or indirectly by foreign investors to undertakings in another economy with the expectation of better profits and also participation in the management of the undertaking in which they invest. In relation to their equity stakes, the international investors gain ownership of properties in the host country companies.

International Monetary Fund (IMF), has defined FDI as "an investment that is made to acquire a lasting interest in an enterprise operating in an economy other than that of the investor" The investor's purpose is to have an effective voice in the management of the enterprise (IMF, 1977). FDI is the mechanism by which citizens of one country (the source country) acquire property ownership for the purpose of regulating a firm's output, distribution and other productive activities in another country (the host nation).In this paper an attempt has made to study the trend and pattern of foreign direct investment in last three decades and correlation is studied between FDI and FPI.

Review of Literature

Dr. Bipul Kumar Das (2020) the study seeks to investigate, especially after 1991, the trend and pattern of FDI inflows to India in the post-independence period. It is found that in the 1990s, FDI inflows showed a big jump and have become more extreme since 2001. Over the years, India's share of world FDI has been rising. Much of the FDI flows through an automated route to India, followed by the purchase of existing shares. In addition, Mauritius, Singapore, the United Kingdom, Japan, the United States, and the Netherlands are the major sources of FDI inflows to India; most of them based on the service and telecommunication sectors.

Deivamani. S, et al. (2018) analyzed the FDI determinants, the sources of FDI inflows in India during the 2016-17 fiscal years. According to the study, the inflow of FDI into the service sector and the construction and development sector achieved sustainable economic growth and development through job creation in India. Thus, in order to make the Indian economy a developed economy, the government must proceed in India to elicit FDI inflows.

Murugesan. B (2016) the trend and growth of FDI inflows in the past liberalization period and the sector-wise FDI inflows received in India-was investigated. This study explored a major effect of FDI on economic growth and sector-specific FDI inflows earned in India between 2006 and 2013. FDI inflows can be used to increase domestic production, exports and save through equal distribution.

Saini, Amit (2015) analyzed the sector-specific pattern in Indian FDI inflows in two separate regimes, 1991-2000 and 2001-2012. Due to the large GDP and GNI, tax incentives and availability of high-quality multilingual workforce, the results show that the highest FDI inflows received in the service sector during the last decade along with Tele-communication sector. .But India's FDI is much smaller than China and other small Asian economies. In order to attract FDI, India needs to build these attractive investment avenues, frame liberal economic policies and improve infrastructure rates in India.

Teli .R.B. (2013) found that the correlation between FDI inflows and other relevant economic indicators such as GDP, trade, etc. is very strong. GOI should take cautionary steps while allowing for various sectors, such as multi-brand retailing in India. Regulatory policies should be strengthened and policymakers should avoid confusion about boosting the FDI line in India and eventually increasing GDP, trade and foreign reserves of the country.

Bhattacharya and Bhattacharya (2011) researched that the amount of trade in goods and FDI inflows affects economic development. The government is preparing more liberalization initiatives across a wide range of sectors (Agriculture, Manufacturing, and Services), which would further speed up FDI inflow. The results show that FDI is growth-enhancing in the same way as domestic investment, and there is statistically significant impact in the sense that a higher ratio of FDI in gross capital formation has positive effects on GDP level and therefore on growth.

Rizvi and Mohammad (2009) revealed that India and China received a substantial amount of foreign direct investment from developed countries, and also significantly increased FDI flows to Pakistan. Implications for FDI policy are expressed in the light of the empirical outcomes. The impact of FDI on employment may vary from industry to industry and the overall insignificant relationship between FDI and growth in employment may reflect a cancelation of the positive and negative impact of FDI flows on employment in different industries.

Objectives

1. To study the trend of the foreign direct investment in India after the liberalization.
2. To study the correlation between Foreign Direct Investment and capital account of India

Collection of Material

This analysis was made using secondary data. The investigator obtained data from different sources that were written, viz. RBI bulletins, World Investment Report (UNCTAD), World Bank, Indian Economy Statistics Handbook (RBI), India Department of Commerce and Industrial Development, etc. Besides these various journals, magazines, articles and books were also consulted in this research paper.

Research Methodology

In this paper, an attempt was made to investigate the trend in FDI inflows and major sources of FDI inflows in India from 1991 to 2019. A descriptive analytical approach was used in this study to recognize the reasons for heavy growth and decline in the cyclic pattern of FDI inflows in India, and further attempt has made to study correlation between FDI and Capital account. Such cycles will help to clarify the clearer picture of India's FDI inflow. Karlpearson's Coefficient of correlation is used to study the relationship between FDI and capital account. In order to find out the growth of the variable over the period, FDI regresses on time (trend term).

Model of basic linear regression as:-

$$\mathbf{Log\ (FDI)t = \alpha + \beta t + \mu,}$$

The trend word that is viewed as an explanatory variable is 't' and log (FDI) is the logarithmic type of total US dollar FDI inflows, which is the variable explained.

A basic regression analysis is carried out and the model is calculated by the OLS method. If the absolute value of the approximate t-statistic turns out to be greater than 2, then we say that over the period, FDI has increased significantly. In order to determine the growth of FDI, the approximate slope coefficient of the trend term (t) is multiplied by 100.

Analysis of Data

Table: 1 Trend and Pattern of FDI inflow In India (1990 to 2000) (Data in US Dollar Millions)

YEAR	FDI INFLOWS	FDI GROWTH RATE	CAGR
1990-91	97	-	
1991-92	129	32.99%	
1992-93	315	144.19%	
1993-94	586	86.03%	
1994-95	1314	124.23%	36%
1995-96	2144	63.17%	
1996-97	2821	31.58%	
1997-98	3557	26.09%	
1998-99	2462	-30.78%	
1999-00	2155	-12.47%	
2000-01	4031	87.05%	
2001-02	6130	52.07%	
2002-03	5095	-16.88%	
2003-04	4322	-15.17%	
2004-05	6052	40.03%	25%
2005-06	8962	48.08%	
2006-07	22826	154.70%	
2007-08	34844	52.65%	
2008-09	41903	20.26%	
2009-10	37746	-9.92%	
2010-11	36047	-4.50%	
2011-12	46552	29.14%	
2012-13	34298	-26.32%	
2013-14	36047	5.10%	6%
2014-15	45147	25.24%	
2015-16	55559	23.06%	
2016-17	60220	8.39%	
2017-18	60974	1.25%	
2018-19	62001	1.68%	
ECGR	21.2		

Source: Compiled from Reserve Bank of India

Constant value	305.47
Reg. coefficient	0.212359425
R-square	0.897613146
F-value	236.7057
P-value	.000

Trend analysis shows that exponential compound annual growth rate in India is 21.2 and CAGR in decade 1991-2000 is 36%, in 2000 to 2010 it is 25 % and in recent decade it is 6%.R square value is 89.7 which shows that during this time period i.e. post liberalization era FDI is explained almost 90%.P- value shows that there is significant relation.

Trend equation of actual data is-

Log FDI=α + β (t) +e

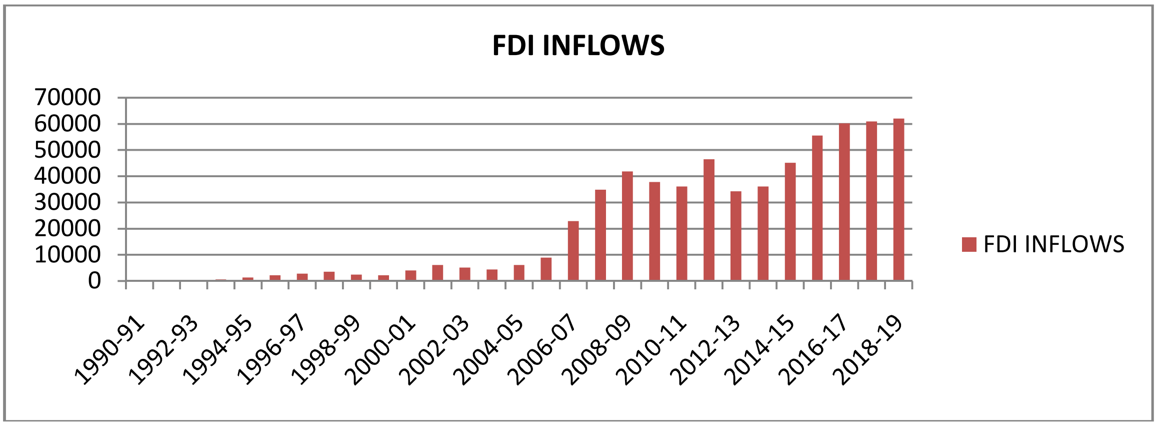

Chart1 FDI inflow In India (1991 to 2019)

From Table 1 we can interpret that FDI inflows in India continuously increased during the early post-liberalization period, i.e. from 1991 to 1997. This increase in FDI inflow may be due to the entry of large numbers of industries or sectors opened up for participation in foreign equity. During 1998-99, the FDI revealed the cyclical trend due to several factors that placed the restriction on FDI inflow in India, such as the adverse effect of India's nuclear test at Pokhran. The second reason was the Indian economy's stagnation due to a moderate recession in both the US and the global economy. The third one concerned adverse external economic factors, such as the South-East Asian financial crisis (P. sahni, 2012). Fourth, the decline was due to the poor domestic industrial environment and political instability.

During 2000 to 2010, the government introduced significant FDI policy reforms and more broad market sizes (Shiralashetti. A.S. and S.S. Huger 2009) attracted foreign investors like Mauritius path, USA, Singapore and Others Confidently to India through FIPB and Automatic routes for reaping huge benefits. India received the highest FDI inflow in 2008 due to a relatively well-developed financial sector, a strong industrial base and a critical mass of well-educated workers (Rajan et. al., 2008). The US financial crisis badly affected the stock market worldwide during the third quarter of Financial Year 2008. The unexpected crisis produced a chaotic situation. India, however, was the least affected country, but it also revealed the slight impact of FDI inflows into India, which tends to lower FDI inflow rates in 2009 and 2010.

India planned to resolve the adverse impact of the financial crisis during 2011 and succeeded in re-inviting significant inflows, but the FDI inflow system moved downward again in 2012. The growth rate of FDI in 2010 and 2012 is negative but it is positive in all other years. FDI introduces modern technologies, transfers knowledge, skill, provides access to export markets along with investment and managerial expertise. In 2014, when India opted for the program "MAKE IN INDIA" to encourage Indian manufacturing FDI rises at a rate of 25%. The key aim of make in India program is to promote the manufacturing sector and protect intellectual property by attracting investors around the globe to invest in India and use India's most skilled labor for the country's growth and development. The initiative aimed at generating jobs for the country's millions of people, and draws foreign direct investment to the country as well. According to Biswajit Dhar, economics professor at Jawaharlal Nehru University, "government had agreed on the sectors under the (Make in India) scheme but these might not be the investors' priority sectors. Where the government plans to invest in manufacturing, it needs to address infrastructural gaps first." So in 2017 FDI growth rate falls and then improve in 2019.

The Share of FDI Inflows in Capital Account of India (1991-2019)

Balance of Payment shows detailed records of all commercial transactions between one country's inhabitants and the rest of the world. The balance of payment is comprised of current and capital account. The capital account consisting of the financial asset transfers in the form of short-term and long-term loans & borrowings and private and official assets. In other words, the capital account shows external loan and investment flows, which reflects a shift in foreign assets and liabilities in the country. Long-term capital flows include international movements of capital with a maturity of one year or more and include direct investments such as the building of a foreign factory, portfolio investment such as the purchasing of foreign bonds and stocks, and international loans. In comparison, short-term international capital transactions span from three months to less than one year. The research (Mohd Nayyer Rahman, 2016) shows that Capital Account Balance and Foreign Direct Investment Inflows are bi-directional causal. This means that Foreign Direct Investment Inflows also affect the Capital Account Balance. Foreign Direct Investment Inflows for an emerging economy such as India is a very critical macroeconomic component.

Table 2 Percentage Share of FDI in the capital account of a country (Amount in crore)

Years	Capital account	Foreign Direct Investment	FDI as % of capital account
1991-92	9509	339	3.56
1992-93	11883	1699	14.29
1993-94	30415	13282	43.66
1994-95	28743	15450	53.75
1995-96	15596	16312	104.59
1996-97	40502	21828	53.89
1997-98	37536	19961	53.17
1998-99	35034	10169	29.02
1999-00	48101	22501	46.77
2000-01	39241	31016	79.03
2001-02	40167	38861	96.74
2002-03	51377	29072	56.58
2003-04	80010	71728	89.64
2004-05	128081	68366	53.377
2005-06	109633	94814	86.48
2006-07	208017	134282	64.55
2007-08	433167	249389	57.57
2008-09	30515	126449	414.38
2009-10	243935	311704	127.78
2010-11	279105	277038	99.25
2011-12	307470	241706	78.61
2012-13	500313	298205	59.60
2013-14	283190	217933	76.95
2014-15	541238	473655	87.513
2015-16	259592	270436	104.17
2016-17	241150	334814	138.84
2017-18	594942	396925	66.71
2018-19	380023	301927	79.44

Source: Handbook of statistics on the Indian economy, RBI, 2018-19.

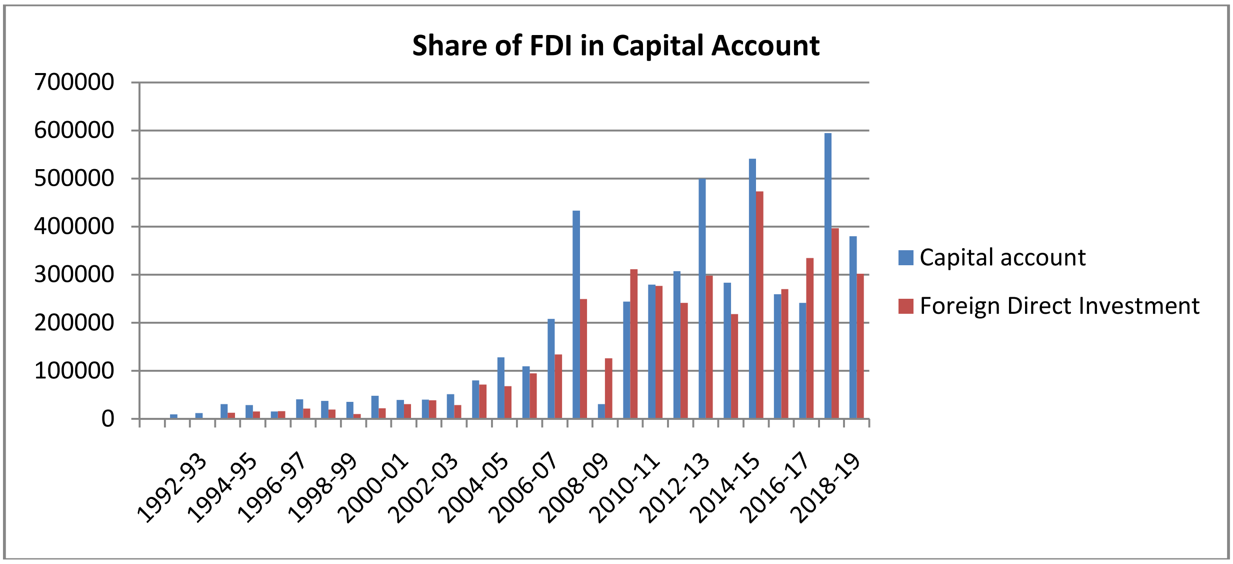

Chart 2Share of FDI in the capital account of a country

The capital account, which includes foreign investment including foreign direct investment and equity flows, overseas borrowing, and banking capital, increased to 380023 million as compared to 9509 million in 1991. It is attributed to a sharp rise in net FDI to 301927 million, which is79.44% of total capital account.

Correlations			
		Capital account	Foreign Direct Investment
Capital account	Pearson Correlation	1	.926**
	Sig. (2-tailed)		.000
	N	28	28
Foreign Direct Investment	Pearson Correlation	.926**	1
	Sig. (2-tailed)	.000	
	N	28	28
**. Correlation is significant at the 0.01 level (2-tailed).			

Result: There is a significant positive correlation relation between FDI and Capital account, r (28) =0.926, p=.000.

Conclusion

After analyzing the trends of last few decades, it has been observed that Foreign Direct Investment in India is increasing with the time but the compound average growth rate is falling. Moreover FDI in India is increasing in absolute terms but relatively it is not up to the mark. There are a variety of factors leading to this contemporary phenomenon with specific reference to being its demographics "with a young population there is a large customer pool to be tapped, the increasing middle class, increased urbanization and visibility, rising disposable income. Now India is opening up its policies to draw international investment inflows even further. The correlation between FDI and capital account is found positive though it is weak.FDI has lasting interest in an economy while FPI is more volatile than FDI. India is now opening its policies to attract inflows of foreign investment even more. Foreign Direct Investment (FDI) is significant growth driver. It is an important source of economic development for the country whereas some people see the threat of FDI to host and domestic business houses' sovereignty.

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