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Problems of Low Fdi Flow to India: A Bird Eye View

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ABSTRACT

FDI refers to capital inflows from abroad that are invested in or to enhance the production capacity of the economy. Despite globalization, the essential role of foreign direct investment (FDI) in economic development has not changed. However, many mechanisms and dynamics of FDI- assisted development have changed: there is greater variation in the kinds of FDI, the benefits each offers, and the manner in which each interacts with the host economy. FDI seen as an important catalyst for economic growth in the developing countries,

KEYWORDS : Foreign Direct Investment, growth, economy,development.

Introduction:

Foreign Direct Investment (FDI) plays a very important role in the development of the nation. It is very much vital in the case of underdeveloped and developing countries. A typical characteristic of these developing and underdeveloped economies is the fact that these economies do not have the needed level of savings and income in order to meet the required level of investment needed to sustain the growth of the economy. In such cases, foreign direct investment plays an important role of bridging the gap between the available resources or funds and the required resources or funds. It plays an important role in the long-term development of a country not only as a source of capital but also for enhancing competitiveness of the domestic economy through transfer of technology, strengthening infrastructure, raising productivity and generating new employment opportunities. In India, FDI is considered as a developmental tool, which helps in achieving self-reliance in various sectors and in overall development of the economy. India after liberalizing and globalizing the economy to the outside world in 1991, there was a massive increase in the flow of foreign direct investment. This paper analyses FDI inflow in to the country during the Post Liberalization period. Further, the trends of FDI inflow into the country are projected for a period of five years from 2010-11 to 2014- 15 using Autoregressive Integrated Moving Average (ARIMA) forecasting technique. The pape r tries to examine the various set of factors which influence the flow of FDI Identifying the causes for low inflow and suggestive remedial measures to increase the flow of FDI in India with that of other developing nations in the world.

FDI Policy in India:

FDI as defined in Dictionary of Economics is investment in a foreign country through the acquisition of a local company or the establishment there of an operation on a new site. To put in simple words, FDI refers to capital inflows from abroad that is invested in or to enhance the production capacity of the economy. Foreign Investment in India is governed by the FDI policy announced by the Government of India and the provision of the Foreign Exchange Management Act (FEMA) 1999. The Reserve Bank of India ('RBI') in this regard had issued a notification, which contains the Foreign Exchange Management (Transfer or issue of security by a person resident outside India) Regulations, 2000. This notification has been amended from time to time. The Ministry of Commerce and Industry, Government of India is the nodal agency for motoring and reviewing the FDI policy on continued basis and changes in sectoral policy/ sectoral equity cap. The FDI policy is notified through Press Notes by the Secretariat for Industrial Assistance (SIA), Department of Industrial Policy and Promotion (DIPP).The foreign investors are free to invest in India, except few sectors/activities, where prior approval from the RBI or Foreign Investment Promotion Board ('FIPB') would be required.

OBJECTIVE OF THE STUDY

To identify the problems relating to inflow of FDI and to make suitable suggestions for attracting m ore FDI inflow to India.

PROBLEMS FOR LOW FDI FLOW TO INDIA

India, the largest democratic country with the second largest population in the world, with rule of law and a highly educated English speaking work force, the country is considered as a safe haven for foreign investors. Yet, India seems to be suffering from a host of self-imposed restrictions and problems regarding opening its markets completely too global investors by implementing full scale economic reforms. Some of the major impediments for India's poor performance in the area of FDI are: political instability, poor infrastructure, confusing tax and tariff policies, Draconian labor laws, well entrenched corruption and governmental regulations.

LACK OF ADEQUATE INFRASTRUCTURE:

It is cited as a major hurdle for FDI inflows into India. This bottleneck in the form of poor infrastructure discourages foreign investors in investing in India. India's age old and biggest infrastructure problem is the supply of electricity. Power cuts are considered as a common problem and many industries are forced to close their business.

STRINGENT LABOR LAWS:

Large firms in India are not allowed to retrench or layoff any workers, or close down the unit without the permission of the state government. These laws protect the workers and thwart legitimate attempts to restructure business. To retrench unnecessary workers, firms require approval from both employees and state governments-approval that is rarely given. Further, Trade Unions extort huge sums from companies through over-generous voluntary retirement schemes.

CORRUPTION:

Corruption is found in nearly every public service, from defense to distribution of subsidized food to the poor people, to the generation and transmission of electric power. Kumar (2000) observes that a combination of legal hurdles, lack of institutional reforms, bureaucratic decision-making and the allegations of corruption at the top have turned foreign investors away from India. States that corruption and misuse of public office for private gain are capable of paralyzing a country's development and diverting its precious resources from public needs of the entire nation. Corruption is against the poor people because it snatches away food from the mouths of the poor. If corruption levels in India come down to those of Scandinavian countries, India's GDP growth will increase by 1.5 per cent and FDI will grow by 12 per cent.

LACK OF DECISION MAKING AUTHORITY WITH THE STATE GOVERNMENTS:

The reform process of liberalizing the economy is concentrated mainly in the Centre and the State Governments are not given much power. In most key infrastructure areas, the central government remains in control. Brazil, China, and Russia are examples where regional governments take the lead in pushing reforms and prompting further actions by the central government.

LIMITED SCALEOF EXPORT PROCESSING ZONES:

India's export processing zones have lacked dynamism because of several reasons, such as their relatively limited scale; the Government's general ambivalence about attracting FDI; the unclear and changing incentive packages attached to the zones; and the power of the central government in the regulation of the zones. India which established its first Export Processing Zone (EPZ) in 1965 has failed to develop the zones when compared to China which took initiative for establishment only in 1980

HIGH CORPORATE TAX RATES:
Corporate tax rates in East Asia are generally in the range of 15 to 30 percent, compared with a rate of 48 percent for foreign companies in India. High corporate tax rate is definitely a major disincentive to foreign corporate investment in India.

INDECISIVE GOVERNMENT AND POLITICAL INSTABILITY:
There were too many anomalies on the government side during past two decades and they are still affecting the direct inflow of FDI in India such as mismanagement and oppression by the different company, which affect the image of the country and also deject the prospective investor, who are very much conscious about safety and constant return on their investment.

SUGGESTIONS FOR INCREASED FLOW OF FDI INTO THE COUNTRY
FLEXIBLE LABOUR LAWS NEEDED :
China gets maximum FDI in the manufacturing sector, which has helped the country become the manufacturing hub of the world. In India the manufacturing sector can grow if infrastructure facilities are improved and labour reforms take place. The country should take initiatives to adopt more flexible labour laws.

RE LOOK AT SECTORAL CAPS:
Though the Government has hiked the sectoral cap for FDI over the years, it is time to revisit issues pertaining to limits in such sectors as coal mining, insurance, real estate, and retail trade, apart from the small-scale sector. Government should allow more investment into the country under automatic route. Reforms like bringing more sectors under the automatic route, increasing the FDI cap and simplifying the procedural delays has to be initiated. There is need to improve SEZs in terms of their size, road and port connectivity, assured power supply and decentralized decision-making.

GEOGRAPHICAL DISPARITIES OF FDI SHOULD BE REMOVED:
The issues of geographical disparities of FDI in India need to address on priority. Many states are making serious efforts to simplify regulations for setting up and operating the industrial units. However, efforts by many state governments are still not encouraging. Even the state like West Bengal which was once called Manchester of India attracts only 1.2% of FDI inflow in the country. West Bengal, Bihar, Jharkhand, Chhattisgarh are endowed with rich minerals but due to lack of proper initiatives by governments of these states, they fail to attract FDI.

PROMOTE GREENFIELD PROJECTS:
India's volume of FDI has increased largely due to Merger and Acquisitions (M&As) rather than large Greenfields projects. M&As not necessarily imply infusion of new capital into a country if it is through reinvested earnings and intra company loans. Business friendly environment must be created on priority to attract large Greenfields projects. Regulations should be simplified so that realization ratio is improved (Percentage of FDI approvals to actual flows). To maximize the benefits of FDI persistently, India should also focus on developing human capital and technology.

DEVELOP DEBT MARKET:
India has a well developed equity market but does not have a well developed debt market. Steps should be taken to improve the depth and liquidity of debt market as many companies may prefer leveraged investment rather than investing their own cash. Therefore it is said that countries with well - developed financial markets tend to benefits significantly from FDI inflows.

EDUCATION SECTOR SHOULD BE OPENED TO FDI:
India has a huge pool of working population. However, due to poor quality primary education and higher education, there is still an acute shortage of talent. FDI in Education Sector is lesser than one percent. By giving the status of primary and higher education in the country, FDI in this sector must be encouraged. However, appropriate measure must be taken to ensure quality education. The issues of commercialization of education, regional gap and structural gap have to be addressed on priority.

STRENGTHEN RESEARCH AND DEVELOPMENT IN THE COUNTRY:
India should consciously work towards attracting greater FDI into R&D as a means of strengthening the country's technological prowess and competitiveness.

CONCLUSION
FDI plays an important role in the long-term development of a country not only as a source of capital but also for enhancing competitiveness of the domestic economy through transfer of technology, strengthening infrastructure, raising productivity and generating new employment opportunities. India emerges as the fifth largest recipient of foreign direct investment across the globe and second largest among all other developing countries . The huge market size, availability of highly skilled human resources, sound economic policy, abundant and diversified natural resources all these factors enable India to attract FDI. Further, it was found that even though there has been increased flow of FDI into the country during the post liberalization period, the global share of FDI in India is very less when it is compared to other developing countries. Lack of proper infrastructure, instable government and political environment, high corporate tax rates and limited export processing zones are considered to be the major problems for low FDI into the country. To overcome this situation, the Government should revise the sectoral cap and bring more sectors under the automatic route. Further, India should sign the agreement of Double Taxation treaties with other countries in order to increase bilateral trade. Therefore, there is an urgent need to adopt innovative policies and good corporate governance practices on par with international standards, by the Government of India, to attract more foreign capital in various sectors of the economy to make India a developed economy.

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