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FDI AND INDIAN ECONOMY-: Issues, Challenges and Prospects in India

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ABSTRACT

In this paper, I have attempted to identify the issues challenges and prospects associated with India's current foreign direct investment regime, and more importantly the other associated factors responsible for India's unattractiveness as an investment location. Despite India offering a large domestic market, rule of law, low labour costs, and a well working democracy, her performance in attracting FDI flows has been far from satisfactory. A restrictive FDI regime, high import tariffs, exit barriers for firms, stringent labour laws, poor quality infrastructure, centralized decision-making processes, and a very limited scale of export processing zones make India an unattractive investment location. On the other hand, Foreign Direct Investment (FDI) as a wholeis the most important driver of growth. It is also an important source of non-debt financial resources for country for economic development. Besides this it is a means of achieving technical know- how and a source for employment generation. Although, many are of the view that FDI is a big threat to the sovereignty of the host and indigenous business houses, & faster consumption of natural resources for making profit, may deprive host from such resources in long run. In between of the debate on pros and cons of FDI, world economy has observed a tremendous change in volume and pattern of FDI. There is a clear cut and intense global competition of FDI. India is not behind this global race of attracting these investments. India is an attractive FDI destination for services but has failed to be a manufacturing hub, which has also a greater economic benefit. FDI though one of the important sources of financing the economic development, but this is not a sufficient solution for poverty eradication, unemployment and many other economic ills. India needs a huge investment to achieve the goals of vision 20-20. The Policy makers also need to ensure full transparency and consistency in making policies along with a comprehensive and strong long-term development strategy.

KEYWORDS Foreign Investment Promotion Board (FIPB), Foreign Direct Investment Growth (FDIG), Impact of FDI on GDP, FDI regime.

INTRODUCTION

FDI gives a win – win situation to the host and the home countries. In fact, both the countries are directly concerned in inviting more and more FDI, as they benefit a lot from these type of investments. The 'home' countries have the advantage of the vast markets opened by industrial growth. On the other side, the 'host' countries are having the advantage to acquire technological and managerial skills and aid domestic savings and foreign exchange. As a result, Foreign Direct Investment (FDI) is now been a vital driver of growth. Many Emerging Market Economies (EMEs) are looking upon FDI as one of the easiest means to satisfy and fulfil their financial, technical, employment generation and competitive efficiency requirements. Gradually they also realized that substantial economic growth is inevitable without global integration of business process. This created opportunities for locational advantages and thus facilitated strategic alliances, joint ventures and collaborations over R & D.

FDI in India: FDI & Economic Growth

Before this, 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. However, researchers could not portray the complete history of FDI pouring in India due to lack of abundant and authentic data. Before independence, major amount of FDI came from the British companies. 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. The first Prime Minister of India considered foreign investment as "necessary" not only to supplement domestic capital but also to secure scientific, technical, and industrial knowledge and capital equipment. However, the country faced two severe crises in the form of foreign exchange and financial resource mobilization during the second five-year plan (1956 -61). Therefore, the government adopted a liberal attitude by allowing more frequent equity participation to foreign enterprises, and to accept equity capital in technical collaborations. 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. The government also provided many incentives such as tax concessions, simplification of licensing procedures and de- reserving some industries such as drugs, aluminium, heavy electrical equipment, fertilizers, etc. in order to further boost the FDI inflows in the country. This liberal attitude of government towards foreign capital lures investors from other advanced countries like USA, Japan, and Germany, etc. But due to significant outflow of foreign reserves in the form of remittances of dividends, profits, royalties etc., the government had 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.The world economy has observed a phenomenal change in volume and pattern of FDI flow from developed nations to EMEs in 1980s and 1990s compared to earlier decades. The hostile attitude of developing nations regarding multinationals investment has become generous during this transition period. FDI was fostered by liberalisation and market-based reforms in EMEs. The financial sector deregulation

and reforms in the industrial policy further paved the way for global investments. Some of the most phenomenal developments during the last 20 years is the fabulous growth of FDI in the global economic arena.Starting from a baseline of less than USD 1 billion in 1990, a recent UNCTAD survey projected India as the second most important FDI destination (after China) for transnational corporations during 2010-2012. As per the data, the sectors which attracted higher inflows were services, telecommunication, construction activities and computer software and hardware. Mauritius, Singapore, the US and the UK were among the leading sources of FDI to the country.In 2013, the government relaxed FDI norms in several sectors, including telecom,defence, PSU oil refineries, power exchanges and stock exchanges, among others. In retail, UK-based Tesco submitted its application to initially invest US$ 110 million to start a supermarket chain in collaboration with Tata Group's Trent. In civil aviation, Malaysia-based Air Asia and Singapore Airlines teamed up with Tata Group to launch two new airline services. Also, Abu Dhabi-based Etihad picked up a 24 per cent stake in Jet Airways that was worth over Rs 2, 000 crores (US$ 319.39 million).Currently, while foreign portfolio investments to India are slowing, net foreign direct investment (FDI) inflows, which are far more stable, have touched a record high of $34.9 billion in 2014-15. In fact, net FDI inflows touched 1.7% of gross domestic product (GDP) in the just-ended fiscal year, up from 1.1% of GDP the previous year. Foreign investment inflows to India are predominantly to infrastructure, mainly telecom, oil and gas, mining sectors, as well as the services sector.Higher FDI flows are good for India's current account deficit and also help drive domestic investments. With the government opening up various sectors such as insurance and defence, these stable flows may continue this year as well.

LITERATURE REVIEW

Review of various literatures available on FDI reveals that foreign investment is still a matter of debate. Whether FDI is boom or bane for host countries economic growth and development? Opinions are still divided. FDI has its own advantages and disadvantages. Many scholars argue that through FDI developed nations may try to invade the sovereignty of host country. In order to earn quick profit, they may exploit the natural resources at the faster rate and thus leave the host country deprived in the long run. Many are of the opinion that basic objective of foreign investments is to earn profits by ignoring the overall social & economic development of the host nation. Thus, an attempt has been made to discuss various issues raised by different scholars on the subject.

Balasubramanyam V.N Sapsford David (2007) in their article "Does India need a lot more FDI" compares the levels of FDI inflows in India and China, and found that FDI in India is one tenth of that of china. The paper also finds that India may not require increased FDI because of the structure and composition of India's manufacturing, service sectors and her endowments of human capital, Also, India has a large pool of well – Trained engineers and scientists capable of adapting and restructuring imported know – how to suit local factor and product market condition all of these factors promote effective spill overs of technology and know- how from foreign firms to locally own firms. The optimum level of FDI, which generates substantial spill overs, enhances learning on the job, and contributes to the growth of productivity, is likely to be much lower in India than in other developing countries including China. Finally, they conclude that the country is now in a position to unbundle the FDI package effectively and rely on sources other than FDI for its requirements of capital.

Nirupam Bajpai and Jeffrey D. Sachs (2006) in their paper "Foreign Direct Investment in India: Issues and Problems", attempted to identify the issues and problems associated with India's current FDI regimes, and more importantly the other associated factors responsible for India's unattractiveness as an investment location. Despite India offering a large domestic market, rule of law, low labour costs, and a well working democracy, her performance in attracting FDI flows have been far from satisfactory.

Kulwinder Singh (2005) in his study "Foreign Direct Investment in India: A Critical analysis of FDI from 1991-2005" explores the uneven beginnings of FDI, in India and examines the developments (economic and political) relating to the trends in two sectors: industry and infrastructure. The study concludes that the impact of the reforms in India on the policy environment for FDI presents a mixed picture. The industrial reforms have gone far, though they need to be supplemented by more infrastructure reforms, which are a critical missing link.

Chandan Chakraborty, Peter Nunnenkamp (2004) in their study "Economic Reforms, FDI and its Economic Effects in India" assess the growth implications of FDI in India by subjecting industry – specific FDI and output data to Granger causality tests within a panel co -integration framework. It turns out that the growth effects of FDI vary widely across sectors. FDI stocks and output are mutually reinforcing in the manufacturing sector. Most strikingly, the study finds only transitory effects of FDI on output in the service sector, which attracted the bulk of FDI in the post – reform era. These differences in the FDI – Growth relationship suggest that FDI is unlikely to work wonders in India if only remaining regulations were relaxed and still more industries opened up o FDI.

Naga Raj R (2003) in his article "Foreign Direct Investment in India since 1990s: Trends and Issues" discusses the trends in FDI in India in the 1990s and compare them with China. The study raises some issues on the effects of the recent investments on the domestic economy. Based on the analytical discussion and comparative experience, the study concludes by suggesting a realistic foreign investment policy.

To sum up, it can be said that large domestic market, cheap labour, human capital, are the main determinants of FDI inflows to India, however, its stringent labour laws, poor quality infrastructure, centralize decision making processes, and a very limited numbers of SEZs make India an unattractive investment location.

OBJECTIVES

- To Study the Current Trends & Issues associated with FDI in Indian Economy.
- To Analyse Problems and give their solutions related to FDI in Indian economy.
- To find out the future prospects of FDI in Indian economy.

RESEARCH METHODOLOGY

This study is of **analytical** nature and makes use of **secondary data**. The required& relevant secondary data are collected from various publications of Government of India, Reserve Bank of India, World Investment Reports, Publications from Ministry of Commerce &from the websites of Dept. of Industrial Policy &Promotions (Govt. of India), World Bank, IMF, WTO, RBI, UNCTAD, etc. The time series data and the relevant data have been collected for the period 1991 to 2015.

FINDINGS AND SUGGESTIONS

CurrentTrends &Issues

India received $19.78 billion (Rs 1.3 lakh crore) FDI in 2014-15 from a dozen major FDI source countries that Prime Minister Mr. Modi has visited since taking over in May last year. This accounts for more than half of the $34.93 billion FDI the country received in the fiscal year, which was 27 per cent more than the year before. FDI grew quicker after the launch of the Make in India programme in September 2014 — inflows jumped 48 per cent between October 2014 and April 2015 over the year-earlier period, data from the Department of Industrial Policy and Planning showed. The ex-mentor of confederation of Indian industries (CII) Tarun Das said about the "Modi govt. and current trends and issues of FDI" – "Modi has been able to integrate foreign policy with economic and corporate policies. India is emerg-

ing as the apple of everybody›s eye as other BRICS economies are witnessing downslide, a big change has been brought in the approach towards foreign investors by the PM deciding to meet individual CEOs of global business giants. When domestic investments are constrained and Indian banks have huge NPAs, FDI is key to boosting economy.»Among the countries that Modi visited, Japan has committed to invest about $35 billion in five years and South Korea about $10 billion. China has assured $20 billion in the next five years, while France has announced $2 billion euros ($2.26 billion). The UAE has assured to pump in money for India›s $75-billion infrastructure fund. The UK has launched a programme for investments here ahead of Modi›s planned trip in November and Germany has also made announcements related to the Make in India initiative during Chancellor Angela Merkel›s visit to New Delhi in the first week of October.

"There has been some questions about the Modi government's performance when it comes to pace of reforms and ease of doing business," a foreign diplomat in Delhi said. But a government official from Japan, one of the countries that Modi visited and from where he got a huge investment commitment, said that there was no major reason to be upset about since Modi became the PM.

Before this, in the last terms during UPA tenure, The Ministry of Home Affairs had finally given the approval to the proposal of allowing FDI in railways. The Cabinet Committee on Economic Affairs (CCEA) was expected to consider the proposal. Foreign investors could invest only in construction and maintenance of railway projects, and not in operations. India's the then Prime Minister Mr Manmohan Singh had sought increased Japanese investment in the country. The two countries were already looking at the possibility of concrete cooperation in areas such as manufacturing and research and development in the electronic industry and energy efficient and energy saving technologies.

Evaluation of FDI and GDP in India during (2000-2001 to 2014-2015).

In the following table,the FDI & its related data are taken from the website of "department of industrial policy and promotions, Ministry of Commerce & Industry, Govt. Of India" & GDP and its related data are collected from RBI's "Handbook on Statistics and Indian Economy". So overall it depicts the picture of FDI inflows & its impact on the GDP of India.

Years	FDI Inflow (Rs. Crores)	FDI Inflow (US Million $)	Growth rate of FDI Inflow	GDPat current prices	Growth rate of GDP	FDI as a % of GDP
	Equity Capital Components Only		(In terms of $)	(In Crores)	(In terms of Rs)	
2000-01	10,733	2463	-	2,000,743	-	0.54
2001-02	18,654	4065	+65	2,175,260	8.72	0.86
2002-03	12,871	2705	-33	2,343,864	7.75	0.55
2003-04	10,064	2188	-19	2,625,819	12.03	0.38
2004-05	14,653	3219	+47	2,971,464	13.16	0.50
2005-06	24,584	5540	+72	3,390,503	14.10	0.72
2006-07	56,390	12,492	+125	3,953,276	16.60	1.43
2007-08	98,642	24,575	+97	4,582,086	15.91	2.15
2008-09	1,42,829	31,396	+28	5,303,567	15.75	2.70
2009-10	1,23,120	25,834	-18	6,108,903	15.18	2.02
2010-11	97,320	21,383	-17	7,248,860	18.66	1.34
2011-12	1,65,146	35,121	+64	8,391,691	15.77	1.97
2012-13	1,21,907	22,423	-36	9,388,876	11.88	1.29
2013-14	1,47,518	24,299	+8	10,472,807	11.54	1.41
2014-15	1,89,107	30,931	+27	11,550,240	10.28	1.64

From the data shown in the table we can verdict that FDI has been increasing with increasing rate except in 2 or 3 years when it had decreased. If we talk comparatively between FDI & GDP, we can say that since 2000-01 to the 2014-15 the impact of FDI on GDP has been vigorous except same in those years when the FDI was down. It also presupposes that the impact may also be more strengthen in the coming years since the regime of FDI has been easing down.

Problems &suggestions for their solutions

In spite of the obvious advantages of FDIs, there are quite a few challenges/problems facing larger FDIs in India. So in order to solve these, few root cause of the problems along with the feasible solutions are given below, such as:

Resource challenge: India is known to have huge amounts of resources. There is manpower and significant availability of fixed and working capital. At the same time, there are some underexploited or unexploited resources. The resources are well available in the rural as well as the urban areas. The focus is to increase infrastructure 10 years down the line, for which the requirement will be an amount of about US$ 150 billion. This is the first step to overcome challenges facing larger FDI.

Equity challenge: India is definitely developing in a much faster pace now than before but in spite of that it can be identified that developments have taken place unevenly. This means that while the more urban areas have been tapped, the poorer sections are inadequately exploited. To get the complete picture of growth, it is essential to make sure that the rural section has more or less the same amount of development as the urbanized ones. Thus, fostering social equality and at the same time, a balanced economic growth.

Political Challenge: The support of the political structure has to be there towards the investing countries abroad. This can be worked out when foreign investors put forward their persuasion for increasing FDI capital in various sectors like banking, and insurance. So, there has to be a common ground between the Parliament and the Foreign countries investing in India. This would increase the reforms in the FDI area of the country.

Federal Challenge: Very important among the major challenges facing larger FDI, is the need to speed up the implementation of policies, rules, and regulations. The vital part is to keep the implementation of policies in all the states of India at par. Thus, asking for equal speed in policy implementation among the states in India is important.

India must also focus on areas of poverty reduction, trade liberalization, and banking and insurance liberalization. Challenges facing larger FDI are not just restricted to the ones mentioned above, because trade relations with foreign investors will always bring in new challenges in investments.

Prospects& future outlook

India is estimated to require around US$ 1 trillion during the 12th Five-Year Plan period (2012–17), to fund infrastructure in sectors such as roads, airports and ports. The government is in the process of liberalising FDI norms in construction activities and railways, which could bring in investments to meet the target. The government is also relaxing FDI norms in other sectors for foreign investors to invest. FDI in multi-brand retail has been allowed up to 51 per cent. The minimum requirement for the FDI is US$ 100 million, of which at least 50 per cent must be invested in 'backend infrastructure' within three years following the initiation of the FDI. FDI limit in single-brand retail has been increased to 100 per cent; 49 per cent will be under the automatic route and the rest through the (Foreign Investment Promotion Board) FIPB route.Except that, amendments in Indian FDI policy recently opened a no. of key business sectors to increased foreign investment & in several instances, eliminated the need for foreign investors to obtain approval from the Indian Govt. before investing. These changes had a profound influence on FDI trends in India.Ultimately the current regime and the future policies that are declared to be adopted soon, shall bring up "GOOD DAYS" for FDI in India as well.

CONCLUSION

India's Foreign Direct Investment (FDI) policy has been grad-

ually liberalised to make the market more investor friendly. The results have been encouraging. These days, the country is consistently ranked among the top three global investment destinations by all international bodies, including the World Bank, according to a United Nations (UN) report. For Indian economy which has tremendous potential, FDI has had a positive impact. FDI inflow supplements domestic capital, as well as technology and skills of existing companies. It also helps to establish new companies. All of these contribute to economic growth of the Indian Economy. FDI off course might be one of the important sources of financing the economic development. However, one should not forget that FDI alone is not a solution for poverty eradication, unemployment and other economic ills. India needs a massive investment to achieve the goals of vision 20-20. Policy makers need to ensure transparency and consistency in policy making along with comprehensive long term development strategy.

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