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An Analytical Study on Foreign Direct Investment and Service Sector in India

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Abstract:
Nowadays, due to the global recession, most of the countries have not been able to raise capital. One of the economic aspects of globalization is increasing investments in the form of Foreign Direct Investments (FDI). They are in search of financial support in order to achieve stability in the economy. India is also looking forward for FDI in order to move in a direction to become a developed economy. India has been able to attract better FDI than other developed countries even during the crisis period and now FDI in India has been showing a positive growth rate. Since 1991 the government has focused on liberalization of policies to welcome FDI as it has been a key driver for accelerating the economic growth through technology transfer, employment generation, and improved access to management expertise, global capital, product markets and distribution network. FDI in India has enabled to achieve a certain degree of financial stability; growth and development to sustain and compete in the global economy. The Services sector has been very crucial for India as their contributions towards GDP growth, services, export growth and openness of the economy is vulnerable. Service sector contributes over 60 per cent to India's GDP. On this backdrop, an attempt is made to analyze FDI and service sector in India and its impact on the growth of the economy. It also focuses on the determinants and need of FDI in Indian economy in general and service sector in particular.

Key words: *FDI, financial stability, GDP, Growth & Development, Indian Economy*

1. Introduction

Developing countries always need financial support in order to achieve stability in the economy. Similarly, India, being a developing country, is looking forward for foreign direct investment in order to move in a direction to become a developed economy. Indian economy is a fast growing economy and it holds highly strong position in global hub as Indian economy registers high growth figures of economy when globally there was a heavy financial meltdown. Due to this growth, investors of overseas are confident and interested to invest in India, which is giving a boost to FDI in India. The early nineties was a period when the Indian economy faced a severe Balance of Payment crisis. In such adverse situations, the policy makers decided to adopt a more liberal and global approaches, thereby, opening its door to FDI inflows in order to restore the confidence of foreign investors. FDI benefits the host countries as well as the home nations. The home countries want to take the advantage of the vast markets opened by industrial growth. Whereas the host countries get to acquire resources ranging from financial, capital, entrepreneurship, technological know-how and managerial skills which assist it in supplementing its domestic savings and foreign exchange. Many foreign investors are interested to invest in India to grab the opportunities in the Indian economy. Both foreign investors and host country are benefitted by FDI flows.

1.1. Trends and patterns of FDI flow in India among the world

Trends in World FDI flows show that developing countries make their presence felt by receiving a considerable chunk of FDI inflows. Developing economies share in total FDI inflows rose from 26 percent in 1980 to 40 percent in 1997. However, the share during 1998 to 2003 fell considerably, but rose in 2004, again in 2006 and 2007 it reduces to 29 percent to 27 percent due to he global economic meltdown. Specifically, developing Asia received 16 percent, Latin America and the Caribbean 8.7 percent, and Africa 2 percent. On the other hand, developed economies show an increasing upward trend of FDI inflows, while developing economies show a downward trend of FDI inflows after 1995. However, India shows a steady pattern of FDI inflows during 1991-2007. The annual growth rate of developed economies was 33 percent, developing economies was 21 percent and India was 17 percent in 2007 over 2006. During 1991-2007 the compound annual growth rate registered by developed economies was 16 percent, developing economies was merely 2 percent, and that of India was 41 percent.

1.2. Entry Routes of FDI

The foreign investors can make their investments in the equity shares/fully, compulsorily and mandatorily convertible debentures/ fully, compulsorily and mandatorily convertible preference shares of an Indian company, through two routes;

- The Automatic Route: Under it, the foreign investors do not require any approval from the Reserve Bank of India or Government of India GOI) for the investment.
- The Government Route: Under it, prior approval of the GOI through the Foreign Investment Promotion Board (FIPB) is required.

Period	Approval Route	Automatic Route	Total
2008-09	6	974	980
2009-10	4	690	694
2010-11	19 z	1187	1206
2011-12*	10	1123	1133

Table 1: Number of proposals under Approval and Automatic Route
*Source: ICRIER Policy Series * April 2011 to 22nd February, 2012*

Table 1 gives the details of a number of proposals under approval and automatic route during the period 2008-12. Over the years, Automatic route has become the most used entry route for FDI investments in India indicating the gradual liberalization of FDI policy.

S. No.	Country	Percentage of cumulative Inflows (in terms of US $)
1	Mauritius	42
2	Singapore	10
3	USA	7
4	UK	6
5	Netherlands	5
6	Japan	4
7	Cyprus	4
8	Germany	2
9	France	2
10	UAE	1
Total FDI inflows		83

Table 2: Top Foreign Investors and FDI inflows
Source: www.fdiindia.in

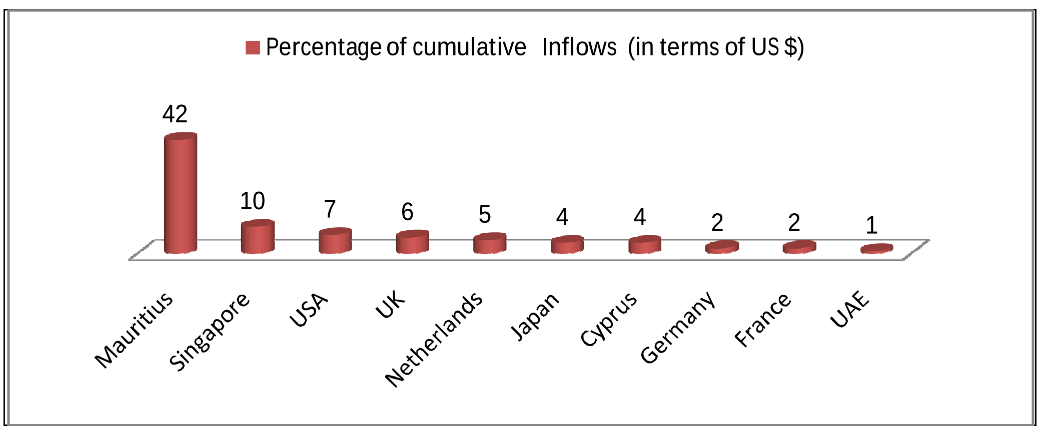

Figure 1: Top Foreign Investors and FDI inflows
Source: www.fdiindia.in

Above table shows that during 2000-10, India has attracted FDI worth 178 billion dollars due to various tax advantages for the international investors. Share of top ten investing countries in India stood at 83 per cent. Mauritius was the top country of origin for FDI flows into India primarily driven by the tax haven status enjoyed by Mauritius.

Table 3 shows the Top ten priority sectors that attracted highest FDI inflows in the country during 2008-11. It depicts that Services sector (Financial & Non-financial) attracted the largest FDI equity flows amounting USD 31 Bn. (20.5 per cent share). Other high share sectors in top ten were - Telecom (8 per cent), Computer Software & Hardware (7 per cent), Housing & Real

Estate (7 per cent) and Construction (7 per cent). Over the years, Automatic route has become the most used entry route for FDI investments in India indicating the gradual liberalization of FDI policy.

Ranks	Sector	2008-09 (April-March)	2009-10 (April-March)	2010-11 (April-March)	Cumulative Inflows (April'00-March'11)	Percentage to total Inflows (in terms of US$)
1	Service sector (financial & non-financial)	28,516 (6,138)	20,776 (4,353)	15,539 (3,403)	120,771 (27,007)	21 %
2	Computer Software & Hardware	7,329 (1,677)	4,351 (919)	3,571 (784)	47,700 (10,723)	8 %
3	Telecommunications (radio paging, cellular mobile, basic telephone services)	11,727 (2,558)	12,338 (2,554)	7,546 (1,665)	48,220 (10,589	8 %
4	Housing & Real Estate	12,621 (2,801)	13,586 (2,844	5,149 (1,127)	43,192 (9,632)	7 %
5	Construction Activities (Including Roads & Highways)	8,792 (2,028)	13,516 (2,862	5,077 (1,125)	40,770 (9,178)	7 %
6	Automobile Industry	5,212 (1,152)	5,754 (1,208)	6,008 (1,331)	26,831 (5,927)	5 %
7	Power	4,382 (985)	6,908 (1,437)	5,709 (1,252)	26,712 (5,900)	5 %
8	Metallurgical Industries	4,157 (961)	1,935 (407)	5,055 (1,105)	18,495 (4,235)	3 %
9	Petroleum & Natural Gas	1,931 (412)	1,328 (272)	2,621 (574)	13,735 (3,153)	2 %
10	Chemicals(Other Than Fertilizers)	3,427 (749)	1,707 (362)	1,810 (398)	13,078 (2,892)	2 %

Table 3: Sectors attracting highest FDI Equity inflows -Amount in Rs. Crores (US $ million)
Source: www.fdiindia.in

Of the ten, service sector had the highest inflow while chemicals sector had the least inflow of 2 percent only. The services sector comprising financial and non-financial services attracted 21 per cent of the total FDI equity inflow into India, with FDI worth US$ 2,853 million during April-December 2010, while telecommunications, including radio paging, cellular mobile and basic telephone services attracted the second largest amount of FDI worth US$ 1,327 million during the same period. Automobile industry was the third highest sector attracting FDI worth US$ 1,066 million, followed by power sector, which garnered US$ 1,028 million during the financial year April-December 2010. The Housing and Real Estate sector received FDI worth US$ 1,024 million. Table below gives the clear picture of FDI inflows for the period during 2000 to now onwards, which shows fluctuations due to various causes such as Govt. policies, fear of investors, political environment of the hosting country, conservative FDI policy and strict rules and guidelines for the investors etc.

S. No.	Financial Year (April- March)	Amount of FDI inflows		Percentage of growth over previous year in terms of US $
		In Rs. Crores	In US $ million	
1	2000-01	10733	2463	
2	2001-02	18654	4065	(+) 65 %
3	2002-03	12871	2705	(-) 33 %
4	2003-04	10064	2188	(-) 19 %
5	2004-05	14653	3219	(+) 47 %
6	2005-06	24584	5540	(+) 72 %
7	2006-07	56390	12492	(+) 125 %
8	2007-08	98642	24575	(+) 97 %
9	2008-09*	142829	31396	(+) 28 %
10	2009-10#	123120	25834	(-) 18 %
11	2010-11#	97320	21383	(-) 17 %
12	2011-12#	165146	35121	(+) 64 %
13	2012-13#	121907	22423	(-) 36 %
Cumulative Total (from April 2000- April 2013)		**909536**	**195725**	**-**

Table 4: FDI equity inflows during 2000-12
Source: www.fdiindia.in

Note:

- Including amount remitted through RBI's – NRI schemes (2000-02)
- FEDAI (Foreign Exchange Dealers Association of India) conversion rate from rupees to US dollar applied, on the basis of monthly average rate provided by RBI
- # figures indicate provisional, subject to reconciliation with RBI
- * An additional amount of US $ 4,035 million pertaining to the year 2008-09, since reported by RBI, has been included in FDI data base from February

India has been ranked at the second place in global foreign direct investments in 2010 and will continue to remain among the top five attractive destinations for international investors during 2010-12 period, according to the United Nations Conference on Trade and Development (UNCTAD) in a report on World Investment Prospects titled, "World Investment Prospects Survey 2009-2012". A report released in February 2010 by Leeds University Business School, commissioned by UK Trade & Investment (UKTI), ranks India among the top three countries where British companies can do better business during 2012-14.

2. Review of Literature

Nowadays, all countries are striving hard to attract FDI by expecting a positive effect on income generation from capital inflows, advanced technology, management skills and market know-how. As FDI is the current burning issue and several researches were conducted on various aspects of it. It is an interesting subject for research scholars and policy makers. The literature review mainly focused on huge untapped areas and the opportunities available in the Indian economy.

FDI has been proved in the literature to be an important promoter of economic growth. Borensztein et al., (1998) opined that FDI is a key ingredient of successful economic growth in developing countries because the very essence of economic development is the rapid and efficient transfer and cross border adoption of best practices, be it managerial and technical best practice or deployment of technology from abroad. Proximity and better access to large market is also well known to attract foreign direct investment that in turn implies often accelerated technology transfer. As such better worker training dispensed by foreign investors has often been argued to raise the level of productivity. Countries can in effect use such firms as catalysts that allow them to leapfrog stages in development. Foreign direct investment can thus speed up the structural shift of the economy. Agosin and Mayer (2000) argued that FDI act as a catalyst for inward investment by complementing local resources and providing a signal of confidence in investment opportunities.

Balasubramanyam et al. (1996) found that in developing countries pursuing outward-oriented trade policies, FDI flows were associated with faster growth than in those developing countries that pursued inward oriented trade policies. Other studies cover only transition economies or industrialized countries covering different periods. Balasubramanyam, Salisu, and Sapsford (1996) and De Mello (1999) interestingly summarized FDI as being a composite bundle of capital stock, know-how, and technology, and can augment the existing stock of knowledge in the recipient economy through labor training, skill acquisition and diffusion, and the introduction of alternative management practices and organizational arrangement. In this context, a recent econometric analysis by Barrell and Pain (1997) found that foreign direct investments' impact on technological change accounted for 30 percent of labour productivity growth in the UK manufacturing sector between 1985 and 1995.

OECD (1996) defines Direct investment involves both the initial transaction between the two entities and all subsequent capital transactions between them and among affiliated enterprise, both incorporated and unincorporated. Geographer Roger Hayter (1997) argues that FDI comprises activities that are controlled and organized by firms (or groups of firms) outside of the nation in which they are headquartered and where their principal decision makers are located. He also points out that FDI involves issues of direct control as resources are transferred internally within firms rather than externally between independent firms. In the case of FDI, parent companies have control over both day to day operations of their investment and their nature and scope in the long run. The International Monetary Fund (1977) defines FDI as "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 being to have an effective voice in the management of the enterprise".

Jones (1998) categorizes FDI in three major types such as:

- Market-seeking – the purpose of the investment is to ensure access to the market of the destination country;
- Resource-seeking – the investment is made to ensure more reliable supplies of natural resources;
- Platform-seeking – the purpose of the investment is to provide a "platform" for production and/or sales activities in a regional market.

Many governments from developed and developing countries believe that FDI can help them get through stagnation and even circumvent the poverty trap (Brooks et al., 2010). Busse and Groizard (2005), the enormous increase in FDI flows across countries is one of the clearest signs of the globalization of the world economy over the past 20 years. Ozturk (2007) viewed that there is a positive association between FDI inflows and growth provided receiving countries have reached a minimum level of educational, technological and/or infrastructure development. Wang (2009) regarded foreign direct investment (FDI) as a factor that drives economic growth.

Hermes and Lensink (2000) interestingly summarized different channels through which positive externalities associated with FDI can occur namely: i) competition channel where increased competition is likely lead to increased productivity, efficiency and investment in human and/or physical capital. Increased competition may lead to changes in the industrial structure towards more competitiveness and more export-oriented activities; ii) training channel through increased training of labour and management; iii) linkages channel whereby foreign investment is often accompanied by technology transfer; such transfers may take place through transactions with foreign firms and iv) domestic firms imitate the more advanced technologies used by foreign firms commonly termed as the demonstration channel.

Shylajan (2011) opined that FDI is considered to be the lifeblood of economic development, especially for the developing and underdeveloped countries. In India, FDI is considered as a developmental tool, which can help in achieving self- reliance in various sectors of the economy. Sharma (2013) expressed that presently in India, 100 per cent FDI is allowed in new projects through the automatic route in the pharmaceutical sector, while 100 per cent is also allowed in existing facilities subject to the government's permission. HSBC Economist Trinh D Nguyen (2013) pointed out that over the past decade, FDI flows have started to shift to ASEAN and India to capitalize on their favourable demographics and fast growth rates. He also said that India's cumbersome business environment, restrictive FDI policy and poor infrastructure can put off foreign investors.

While the literature largely discussed the importance of FDI to growth, one should also realize that economic growth could be an important factor in attracting FDI flows as well. The importance of economic growth to attracting FDI is closely linked to the fact that FDI tends to be an important component of investing firms' strategic decisions. The FDI inflow differential and economic growth disparity among developing countries have created much research interest among economists. There is a large body of theoretical and empirical literature on the impact of FDI on economic growth. It can be viewed that FDI can be expected to benefit the host country by transferring resources, increasing employment opportunities, improving the balance of payments and transferring technology. Researchers such as Findlay, Lall, Loungani and Razin, and Romer noted that FDI brings much needed physical capital, new technology, managerial and marketing talents and expertise, international best practices of doing business as well as increased competition.

3. Database and Methodology

Recently the Government of India (GOI) has placed considerable importance to FDI inflows by liberalizing its' trade and economic policies. India has adopted overwhelming reforms in FDI policy and encouraged inflows into all major sectors of the economy. Hence an attempt has made to analyze the importance of FDI in the service sector, which would provide first-hand empirical evidence on whether further efforts in promoting FDI are warranted. The general objective of the study is to analyze the role of FDI in the service sector in acceleration of the fast growth of Indian economy.

3.1. Objectives of the Study

Many researchers have undertaken the study of different aspects of FDI, formulated conclusions and recommended various suggestions to enhance FDI inflows. Even then certain gaps still remained as FDI is a wide and powerful concept. In order to fill the uncovered gaps, the present study was undertaken to make the study more meaningful and purposeful. With this background the present study "AN ANALYTICAL STUDY ON FOREIGN DIRECT INVESTMENT AND SERVICE SECTOR IN INDIA" has been formulated with the following objectives:

- To study the present scenario of the service sector
- To analyze the need of FDI in this sector.
- To analyze the positive and negative impacts of the reforms to be undertaken.
- To assess the market situations for the same changes in other countries.
- To review the challenges to be faced by Foreign Direct Investors while investing in India.
- To evaluate the changes in the service sector after introduction of FDI

This research is descriptive study in nature. For accomplishing the objectives of the study, both secondary and primary data have been utilized. To evaluate the overall position of the entry of FDI in the economy, mostly secondary data is used which has been collected from various published sources and websites. It has been collected from Publications and websites of GOI, Publications of Planning Department, DIPP, Ministry of Commerce and Industry, Indiastat etc., existing literature and other scholarly works.

Consistent with the objectives of the study, different techniques have been used for the analysis of data. The data was presented through tables and figures and analyzed by using simple statistical techniques of analysis viz., percentages etc. Interpretation of data is based on rigorous exercises aiming at the achievement of the study objectives and findings of the existing studies. Interpretation of the data is more about qualitative terms than on quantitative terms.

3.2. Significance of the Study

The present study is a significant attempt to examine the role of FDI on Indian economy. It will prove helpful to analyze lacunae in the existing economy, problems and shortcomings in the field of infrastructure development, quantity of FDI etc. The study will also prove helpful in enhancing the GDP, earnings of foreign exchange, generating employment avenues and making the country self-reliant. The study may also be equally important for all those interested in undertaking similar studies in the context of other aspects of FDI because certain methods and approaches evolved and employed should be helpful in carrying out further studies of similar nature. The present study is likely to provide valuable information to the government and policy makers about the role of FDI in the growth of the economy. The constraints faced and suggestions made by the study will be of immense help for policy makers and development programme initiators to plan the future programmes most effectively.

4. Discussion

Foreign Direct Investment is one of the measures of growing economic globalization. Investment has always been an issue for the developing economies such as India. The world has been globalizing and all the countries are liberalizing their policies for welcoming investment from countries which are abundant in capital resources. The countries which are developed are focusing on new markets where there is availability of abundant labourer, scope for products, and high profits are achieved. Therefore FDI has become a battle ground in the emerging markets. The objective behind allowing FDI is to complement and supplement domestic investment, for achieving a higher level of economic development and providing opportunities for technological up gradation, as well as access to global managerial skills and practices.

The services sector covers a wide array of activities ranging from services provided by the most sophisticated sectors like telecommunications, satellite mapping, and computer software to simple services like those performed by the barber, the carpenter, and the plumber; highly capital-intensive activities like civil aviation and shipping to employment-oriented activities like tourism, real estate, and housing; infrastructure-related activities like railways, roadways, and ports to social sector related activities like health and education. The National Accounts classification of the services sector incorporates trade, hotels, and restaurants; transport, storage, and communication; financing, insurance, real estate, and business services; and community, social, and personal services. It includes Financial, Banking, Insurance, Non-Financial / Business, Outsourcing, R&D, Courier, Technical testing and analysis etc. In the World Trade Organization (WTO) list of services and the Reserve Bank of India (RBI) classification, construction is also included.

The service sector plays a vital role in India by contributing a major share to national GDP. Over the last two decades, the primary importance of the service sector in the growth process of India and most of the states of India has been strongly established. The growth of the service sector was 9.7 percent with its share in GDP at 57.3 percent. The liberalization of trade and economic policies enabled service sector a remarkable growth rate i.e., 27.4 percent during 2000-01 to 52.1 percent during 2008-09. Some services such as software, tourism, travel related services, transport services, infrastructure and financial services etc. contributed a major share towards the exports of India.

4.1. Investment Scenario

After 1990s due to the liberalized policies of the Government, India has become a favourite place for foreign investors in order to grab the opportunities in the economy. India's economic reforms have generated strong interest in foreign investors to make their investments in India. According to A.T. Kearney report, India ranks second in the World in terms of attractiveness for FDI. A.T. Kearney's 2007 Global Services Locations Index ranks India as the most preferred destination in terms of financial attractiveness, people and skills availability and business environment. Similarly, UNCTAD World Investment Report, 2005 considers India the 2nd most attractive destination among the TNCS. The positive perceptions among investors as a result of strong economic fundamentals driven by 18 years of reforms have helped FDI inflows grow significantly in India.

Cumulative FDI inflows in Services sector:

Cumulative FDI equity inflows (remittance-wise) received during January, 2000 – December, 2011 were Rs. 747,985.14 crores (US$ 165.68 billion). Out of this, the amount of FDI inflows in the Services Sector during January, 2000 to December, 2011 is Rs. 142,637.67 crores (US$ 31.73 billion) which is 19.15 percent of the total FDI inflows. During the period from January, 2000 to December, 2011, cumulative FDI inflows are received from FIPB/SIA, acquisition of existing shares and RBI's automatic routes only.

Sub Sectors	**Amount of FDI inflows**		**Percentage with total FDI inflows**
	Rupees in Crores	**US $ in million**	
Financial	57,950.30	13,059.00	7.88
Banking Services	13,618.75	3,127.94	1.89
Insurance	12,979.49	2,812.25	1.70
Non-Financial Services/Business Services	35,537.55	7,742.59	4.67
Outsourcing	5,607.29	1,225.03	0.74
Research & Development (R&D)	1,382.37	318.10	0.19
Courier	1,703.25	383.79	0.23
Technical testing and analysis	346.87	77.56	0.05
Other Services	13,511.80	2,986.52	1.80
Total	**142,637.67**	**31,732.79**	**19.15**

Table 5: Sub sectors of FDI equity inflows in services sector (from January, 2000 to December, 2011)
Source: www.fdinic.in

Table 4 depicts the sub sectors of FDI equity inflows in service sector during the period January 2000 to December 2011. It reveals that the total inflows is 19.15 percent where as financial sector received highest flow of 7.88 percent and technical testing and analysis received a least of 0.05 percent.

Ranks	Country	Amount of FDI inflows		Percentage with FDI inflows for Services Sector
		Rupees in Crores	**US $ in million**	
1.	Mauritius	56,520.95	12,603.94	39.72
2.	Singapore	22,070.65	4,875.28	15.36
3.	United Kingdom	12,023.29	2,714.82	8.56
4	U.S.A	10,416.33	2,282.70	7.19
5.	Japan	6,855.72	1,434.53	4.52
Total		**107,886.94**	**23,911.27**	**75.35**

Table 6: Share of top five countries attracting FDI inflows for Services sector (from January, 2000 to December, 2011)
Source: www.fdinic.in

Note:

- Amount includes the inflows received through FIPB/SIA route, acquisition of existing shares & RBI's automatic route only; and
- The amount of FDI inflows in respect of the Country & Sector specific data is not provided by RBI, Mumbai prior to January, 2000.

Table 5 gives the top five countries in the world that are contributing to the service sector. The five countries are contributing a total of 75.35 percent towards service sector. Of it, Mauritius is contributing the highest share of 39.72 percent and Japan is contributing lowest of 4.52 percent.

Rank	RBI's Regional Office	States Covered	Amount of FDI inflows		Percentage with FDI inflows for Services Sector
			Rupees in Crores	**US $ in million**	
1.	Mumbai	Maharashtra, Dadra & Nagar Haveli, Daman & Diu	79,141.29	17,622.54	55.53
2.	New Delhi	Delhi, part of UP and Haryana	21,131.98	4,622.79	14.57
3.	Bangalore	Karnataka	5,679.14	1,275.09	4.02
4.	Ahmadabad	Gujarat	2,954.84	712.28	2.24
5.	Hyderabad	Andhra Pradesh	2,879.60	638.66	2.01
Total of above			111,786.85	24,871.36	78.37

Table 7: Share of top five RBI's region-wise (with states covered) in FDI inflows for Service sector (from January, 2000 to December, 2011)
Source: www.fdinic.in

Note:

- Amount includes the inflows received through FIPB/SIA route, acquisition of existing shares & RBI's automatic route only; and
- The amount of FDI inflows in respect of the Country & Sector specific data is not provided by RBI, Mumbai prior to January, 2000.

Table 6 gives the details of the top five states covered in India and FDI s share in the service sector. Maharashtra occupies the first place in FDI inflows in the service sector where as Andhra Pradesh is in last with 2.01 percent.

Services sector is particularly important for India as it contributes a major share in the trend rate of GDP growth. Even in 2008-09 when GDP growth was relatively lower at 6.7 per cent due to global recession, services growth was at 9.7 per cent with its share in GDP at 57.3 per cent. The primary importance of the services sector in the growth process of India and most of the states of India has been strongly established in the last two decades. India is also moving towards a service dominated export growth. Even in 2008-09 when the merchandise export sector was severely affected by the global recession, services exports grew by a respectable 12.5 percent. The openness of the Economy reflected by total trade, including services as a percentage of GDP shows a remarkable increase from 27.4 percent in 2000-01 to 52.1 percent in 2008-09. Some services have been particularly important for India. Software, Tourism and travel related services and transport services are major items in India's Services exports. Besides these, the potential services which are particularly important for India include many professional services, infrastructure related services and financial services. India also has great potential to be a major outsourcing destination for many services.

4.2. Major Policy Issues

The major policy issues in the services sector are:

1) The Domestic Policy Issues including FDI, Disinvestment, Tariff &Tax Issues, Credit & Finance related issues and Other Policy Issues – General & Sector Specific

2) Domestic Regulations-Sector Specific and General

3) Market Access Issues due to domestic regulations, subsidies and other barriers

4) Other Issues like bilateral, regional and multilateral negotiations and policies of multilateral institutions.

- Domestic Policy Issues: Some important policy issues in the case of FDI in Services sector is essential such as raising FDI cap in the insurance sector, liberalization of FDI for banking and animation studios, 100 percent FDI is allowed under automatic route in construction sector, Media and TV channels, railways and other transport services, etc. There is plenty of scope for disinvestment in the case of Public Sector Units (PSUs) in services sector under both the Central and State governments. Around 27 PSU's in Services sector can be considered for disinvestment.
- Domestic Regulations: One major issue in services is the domestic regulations in India. Since domestic regulations perform the role of tariffs in regulating services, domestic regulations need to be disciplined to help the growth of the sector and exports, while retaining those domestic regulations which need to be retained at this stage.
- Market access issues: This is another important issue as domestic regulations and policies in India's major services markets deny market access for India's services exports. Market access barriers can be due to domestic regulations, subsidies or other barriers.
- Services Export Growth: India is also moving to a service dominated export growth with services export growth at 28.0 percent and 22.1 percent respectively for the years 2006-07 and 2007-08. The CAGR for export of services at 28.7 percent is higher than the 19 percent for merchandise exports during 2000-01 to 2006-07. Even in 2008-09 when the world economy was affected by the global recession, India's services exports grew by 12.5 percent. In the second half of 2008-09 export growth of services was less negative at -0.53 percent compared to merchandise export growth of -16.6 percent. However, in the first half of 2009-10, the impact of global recession was visible on India's services export sector as well, with exports declining by 21.4 percent though it was better than the fall of merchandise exports by 28.5 percent. Exports of services are valued at $ 102 billion compared to $185.3 billion of merchandise exports in 2008-09, thus forming 55 percent of merchandise exports.
- Openness of the Economy: Total trade, including services as a percentage of GDP shows a remarkable increase from 27.4 percent in 2000-01 to 52.1 percent in 2008-09. The ratio of services exports to GDP shows an upward movement since 1997-98 which was particularly sharp from 2003-04 to 2006-07.

According to the Department of Industrial Policy and Promotion (DIPP) Foreign Direct Investment (FDI) inflows into the services sector declined by 3.5 per cent to USD 4.66 billion during the April-January period of last fiscal. The financial and non-financial services sector had attracted FDI worth USD 4.83 billion during the same period in the previous year. According to the financial analysts, "The global economic situation is still not healthy. Investors are hesitant to invest their money in the sector". As far as overall FDI inflows are concerned, during the April-January period of 2012-13, it declined by 39 per cent to $19.10 billion. In 2011-12, foreign investment in the services rose to $ 5.21 billion from $ 3.29 billion in 2010-11. Service sector contributes over 60 per cent to India's GDP. The other sectors which have received FDI during April-January 2012-13 include hotel and tourism ($ 3.19 billion), metallurgy ($ 1.38 billion), construction ($ 1.2 billion) and drugs ($ 1 billion).

India received maximum FDI from Mauritius ($ 8.17 billion), followed by Japan ($ 1.69 billion), Singapore ($ 1.82 billion), the Netherlands ($ 1.51 billion) and the UK ($ 1.04 billion). Foreign investments are considered crucial for India, which needs around $ 1 trillion in the next five years to overhaul its infrastructure sector, such as ports, airports and highways to boost growth. The decline in foreign investments could affect the country's Balance of Payments (BoP) situation and also impact the rupee. The insurance sector was given a confidence boost with the FDI limit being raised to 49 percent from 26 percent through the automatic route, but this proposal will need parliamentary approval. Asset reconstruction companies will be allowed 100 percent FDI, with 49 percent through the automatic route from the existing 74 percent through the FIPB route.

The services sector comprising financial and non-financial services attracted 21 per cent of the total FDI equity inflow into India, with FDI worth US$ 2,853 million during April-December 2010, while telecommunications, including radio paging, cellular mobile and basic telephone services attracted the second largest amount of FDI worth US$ 1,327 million during the same period. Automobile industry was the third highest sector attracting FDI worth US$ 1,066 million, followed by power sector, which garnered US$ 1,028 million during the financial year April-December 2010. The Housing and Real Estate sector received FDI worth US$ 1,024 million. During April-December 2010, Mauritius has led investors into India with US$ 5,746 million worth of FDI comprising 42 per cent of the total FDI equity inflows into the country. The FDI equity inflows in Mauritius are followed by Singapore at US$ 1,449 million and the US with US$ 1,055 million, according to data released by DIPP.

India presents a vast potential for overseas investment and is actively encouraging the entrance of foreign players into the market. India is also one of the few markets in the world, which offers high prospects for growth and earning potential in practically all areas of business.

India's FDI inflows into the services sector increased by a mere 5 per cent to $3.6 billion during the April-October period of this fiscal, according to the latest data of industry ministry. The financial and non-financial services sector had attracted FDI worth $3.42 billion during the same period last year. As far as overall FDI inflows are concerned, they declined by about 27 per during the first seven months of the current financial year to $14.78 billion, from $20.29 billion in the year-ago period. Under the extant Foreign Direct Investment (FDI) policy, FDI up to 100 percent is allowed under the automatic route in most sectors/activities, except a few, where sectoral equity/entry route restrictions have been retained. FDI, under the automatic route, does not require any approval and only involves intimation to the Reserve Bank of India within 30 days of inward remittances and/or issue of shares to non-residents.

The growth of the services sector is closely linked to the FDI inflows into this sector and the role of transnational firms. While the ambiguity in classifying the different activities under the services sector continues, the combined FDI share of financial and non-financial services, construction, development, telecommunications, computer hardware and software, and hotel and tourism can be taken as a rough estimate of the FDI share of services, though it could include some non-service elements. This share is 47 per cent of the cumulative FDI equity inflows during the period April 2000- November 2012. The five service sectors are also the sectors attracting the highest cumulative FDI inflows to the economy with financial and nonfinancial services topping the list at US$ 36.04 billion during the period April 2000-November 2012. This is followed by other service sectors: construction development (US$21.77 billion), telecommunication (US $12.62 billion), and computer software and hardware (US $ 11.54 billion). If the shares of some other services or service-related sectors like trading (1.96 per cent), information and broadcasting (1.65 per cent), consultancy services (1.11 per cent), construction (infrastructure) activities (1.06), ports (0.88 per cent), agriculture services (0.80 per cent), hospital and diagnostic centres (0.82 per cent), education (0.36 per cent), air transport including air freight (0.24 per cent), and retail trading (0.02 percent) are included then the total share of cumulative FDI inflows to the services sector would be 56.08 per cent. In 2011-12, FDI inflows to the services sector (top five sectors including construction) grew robustly at 57.62 per cent to US $ 12.14 billion compared to the growth of overall FDI inflows at 33.6 per cent. However, in 2012-13 (April-November), overall FDI inflows fell by 43.3 per cent to US$ 15.85 billion from US$ 27.93 billion in the corresponding period of the previous year. Following this trend, FDI inflows in the top five services also fell by 9.7 per cent to US $ 8.19 billion. Among them, while FDI inflows to the top four services sectors fell in the range of 14 to 97 per cent, FDI inflows to the hotel and tourism sector increased by a very high 328 per cent over the corresponding period in the previous year.

The government has taken many policy initiatives to liberalize the FDI policy for the services sector. These include liberalizing the policy on foreign investment for companies operating in the broadcasting sector, like increasing the foreign investment limit from 49 per cent to 74 per cent in teleports (setting up up-linking HUBs/teleports) and Direct To Home (DTH) and cable networks, and permitting foreign investment (FI) up to 74 per cent in mobile TV; permitting foreign airlines to make foreign investment, up to 49 per cent in scheduled and non-scheduled air transport services; permitting FDI, up to 51 per cent, in multi brand retail trading, and amendment of the existing policy on FDI in single-brand product retail trading.

5. Conclusion

The important services in India include trade, tourism, shipping and port services, real estate services, business services including IT and IT enabled services (ITES), research and development (R&D) services, legal services, and accounting and audit services. Top 10 sectors attracting highest FDI inflows during 2012 were: Services Sector (19 per cent), Construction development: Townships, housing, built-up infrastructure (12 per cent), Telecommunications (7 per cent), Computer Software & Hardware (6 per cent), Drugs & Pharmaceuticals (5 per cent),Chemicals (other than Fertilizers) (5 per cent), Power (4 per cent), Automobile Industry (4 per cent), Metallurgical Industries (4 per cent), Hotel & Tourism (3 per cent). Amount of FDI inflows for the financial year 2012 was US$ 1.1 billion and for the financial year 2012-was estimated at US$ 27.19 billion. Cumulative Amount of FDI Equity Inflows from April, 2000 to December, 2012 was recorded at US$ 187.80 billion.

This paper focuses on various aspects of FDI, determinants and need of FDI in India. India has managed to show a positive GDP growth even during the recession period by liberalizing its FDI policy. According to UNCTAD in its World Investment Report 2010 "If the situation continues to improve, India is likely to be among the most promising investor-home countries in 2010-12 as well as the third highest economy for FDI in 2010-12". India has all the variables such as fine infrastructure, potential markets, abundant labour, availability of natural resources, and at last the economic and trade policies which has been favoring FDI. India is now rated as the second-most favoured destination for FDI in the world after China, but it is expected that in future India would out beet china as it is the fastest growing economy with huge young workforce. Against this backdrop, it is pertinent to highlight the number of measures announced by the Government of India on 1st April, 2011 to further liberalize the FDI policy to promote FDI inflows to India.

In view of the above, allowing FDI in service sector will lead to a significant improvement in India's GDP and overall economic development. The Policy of FDI by the Indian Government would bring improvements in rural infrastructure, technology, price for agricultural produce and employment opportunities. Evidences from various literature reviews indicate that the emergence of giant Foreign Institutional Investors would lead to extensive growth in the Indian Service Sector. By the new policy of FDI, the Indian service sector will get additional benefits and focus on intermediaries and create more jobs for skilled employees in the country. Over the last decade, the fast pace of economic growth and progressive policy liberalization has made India an attractive destination for world's investments. Hence it can be concluded that India's FDI policy has progressively evolved into more and more liberal to enter into any sector of the economy. The study makes clear that the service sector has been the most preferred sector for FDI, which enables to realize India its true potential of economic growth on world's arena. Finally, it can be concluded that Foreign Direct Investment (FDI) gives a kick start to the economy of India, which in turns affects the Service sector in a positive way.

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