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A Study of Flow and Trends of FDI in the Indian Economy

Ritika Ahuja
Assistant Professor, Maitreyi College, University of Delhi, India

Abstract:
One of the most striking developments during the last two decades is the spectacular growth of FDI in the global economic landscape. FDI provides a win – win situation to the host and the home countries. Both countries are directly interested in inviting FDI, because they benefit a lot from such type of investment. Even though India has been a latecomer to the FDI scene compared to other East Asian countries, its considerable market potential and a liberalized policy regime has sustained its attraction as a favourable destination for foreign investors. FDI helps in transferring of financial resources, technology and innovative and improved management techniques along with raising productivity. The objective of the present paper is to provide a broad outline on foreign direct investment with the context of different sectors. The present study has focused on the trends of FDI Flow in India during 2000-01 to 2013-14 (up to November, 2013). The study is based on Secondary data which have been collected through reports of the Ministry of Commerce and Industry, Department of Industrial Promotion and Policy, Government of India,Reserve Bank of India, and World Investment Report.

Keywords: *Foreign direct investment, economic growth, finance, productivity, sectors*

1. Introduction

Foreign direct investment (FDI) is a controlling ownership in a business enterprise in one country by an entity based in another country.Foreign direct investments differ substantially from indirect investments such as portfolio flows, wherein overseas institutions invest in equities listed on a nation's stock exchange. Entities making direct investments typically have a significant degree of influence and control over the company into which the investment is made.The investing company may make its overseas investment in a number of ways - either by setting up a subsidiary or associate company in the foreign country, by acquiring shares of an overseas company, or through a merger or joint venture. The accepted threshold for a foreign direct investment relationship, as defined by the OECD, is 10%. That is, the foreign investor must own at least 10% or more of the voting stock or ordinary shares of the investee company. FDI is a major source of external finance which means that countries with limited amounts of capital can receive finance beyond national borders from wealthier countries. India is the country of potentiality and that is the One of the most prominent and striking feature for today's globalised world. But we have a scarcity of resources .When scarcity meet with resources (FDI) then scope of growth and development emerged. In the last two decades the pace of FDI flows are rising faster than almost all other indicators of economic activity worldwide. Developing countries considered FDI as the safest type of external finance as it not only supplement domestic savings, foreign reserves but promotes growth even more through spillovers of technology, skills, increased innovative capacity, and domestic competition. Now a day, FDI has become an instrument of international economic integration. Located in South Asia, India is the 7th largest, and the 2nd most populated country in the world. With the initiation of new economic policy in 1991 and subsequent reforms process, India has witnessed a change in the flow and direction of foreign direct investment (FDI) into the country. This is mainly due to the removal of restrictive and regulated practices. Foreign direct investment in India increased from US $ 129 millions in 1991-92 to US $ 40,885 million in March, 2005, and US$ above 1, 00,000 million in 2010 an increase of about 1026 times.Presently India is contributing about 17% of world total population but the share of GDP to world GDP is 2%. India has been ranked at the second place in global foreign direct investments in 2010. According to the fact sheet on foreign direct investment dated October 2010, Mauritius is the highest FDI investment in equity inflows with 42% of the total inflow followed by Singapore, USA, UK and Netherlands with 9%, 7%, 5% and 4% respectively. Service sector is the highest FDI attracting inflows with 21% of the total inflows, followed by computer software and hardware, telecommunication and housing and real estate with 9%, 8%, 7% and 7% inflows respectively. 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. According to Ernst and Young's 2010 European Attractiveness Survey, India is ranked as the fourth most attractive foreign direct investment destination in 2010.However, it is ranked the 2nd most attractive destination following China in the next three years.

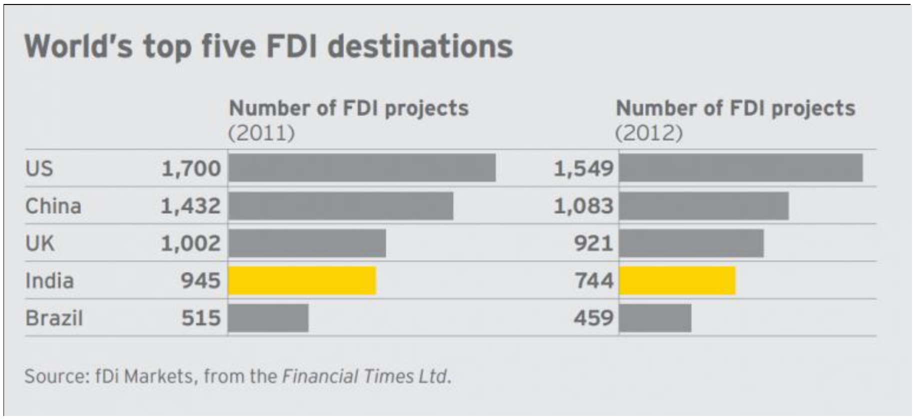

Figure 1: Worlds top 5 FDI destinations

As per statistics from the Department of Industrial Policy & Promotion (DIPP) under theMinistry of Commerce and Industry, CUMULATIVE AMOUNT OF FDI FLOWS INTO INDIA (from April 2000 to May 2010) are US$ 1,68,943 million And CUMULATIVE AMOUNT OF FDI EQUITY INFLOWS (from August 1991 to May 2010) are at US$ 1,36,855 million. According to theWorld Bank, FDI and small business growth are the two critical elements in developing the private sector in lower-income economies and reducing poverty.The most profound effect of FDI has been seen in developing countries, where yearly foreign direct investment flows have increased from an average of less than $10 billion in the 1970's to a yearly average of less than $20 billion in the 1980's, to explode in the 1990s from $26.7billion in 1990 to $179 billion in 1998 and $208 billion in 1999 and now comprise a large portion of global FDI (Source: UNCTAD). FDI inflows into India grew 17 per cent to $28 billion in 2013 despite unexpected capital outflows in the middle of the year, according to a United Nations report. Also, foreign direct investment across the world rose to the levels not seen since the start of the global economic crisis in 2008. India ranked 16th among the top 20 global economies, receiving the maximum FDI. Global FDI increased by 11 per cent to an estimated $1.46 trillion in 2013, with the lion's share going to developing countries, according to the UN Conference on Trade and Development (UNCTAD) report.

An Indian company may receive Foreign Direct Investment under the two routes as given under:

- Automatic Route: FDI in sectors /activities to the extent permitted under the automatic route does not require any prior approval either of the Government or the Reserve Bank of India.
- Government Route: FDI in activities not covered under the automatic route requires prior approval of the Government which are considered by the Foreign Investment Promotion Board (FIPB), Department of Economic Affairs, Ministry of Finance.

➢ FDI is not permitted in the following industrial sectors:

- Arms and ammunition.
- Atomic Energy.
- Railway Transport.
- Coal and lignite.
- Mining of iron, manganese, chrome, gypsum, sulphur, gold, diamonds, copper, zinc.
- Lottery Business
- Gambling and Betting
- Business of Chit Fund
- Agricultural (excluding Floriculture, Horticulture, Development of seeds, Animal Husbandry, Pisciculture and cultivation of vegetables, mushrooms, etc. under controlled conditions and services related to agro and allied sectors) and Plantations activities (other than Tea Plantations) .
- Housing and Real Estate business.
- Trading in Transferable Development Rights (TDRs).
- Manufacture of cigars, cheroots, cigarillos and cigarettes, of tobacco or of tobacco substitutes.

➢ Some Examples of companies that have foreign investors

Foreign investment up to 49% of their paid-up capital:

- Hindustan Unilever Ltd
- HDFC Bank Ltd
- Reliance Industries Ltd
- Reliance Petroleum Ltd
- Zee Telefilms
- Foreign investment up to 40% of their paid-up capital:
- Balaji
- Hero Honda

Foreign investment up to 30% of their paid up capital:

- Asian Paints India Ltd.
- Ranbaxy Laboratories Ltd.
- Gujarat Ambuja Cements Ltd.
- Infotech Enterprises Ltd

2. Review of Literature

- BHAVYA MALHOTRAfinds that India's Foreign Direct Investment (FDI) policy has been gradually liberalised to make the market more investor friendly. He added that 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. He added that It also helps to establish new companies. All of these contribute to economic growth of the Indian Economy.
- DR. SHEETAL MUNDRAA, MUKESH MUNDRAB AND DR. MANJU SINGHattempts to find that FDI has proved to stimulate growth and development of the countries. In addition to direct capital financing, FDI can be a source of valuable technology and know-how while fostering linkages with local firms, which can help jumpstart an economy. In order to promote competitive markets, restrictions on FDI must be reduced. FDI's potential for impact can be greater because of the combination of scale, capital, and global capabilities which allow MNCs to close existing large productivity gaps more aggressively. He added that the Indian retail industry is witnessing large and far reaching changes in last 2 decades of development. Many big Indian corporate have already build significant businesses in different format and sectors of retail. The modernization process started by modern retailers has made positive impact on independent retailers who have also upgraded in terms of assortment, delivery and ambience.
- SHALINI AGGARWAL , ANKUSH SINGLA AND RITU AGGARWALhave observed from their analysis that at the sectoral level of the Indian economy, FDI has helped to raise the output, productivity and employment in some sectors especially in service sector. Indian service sector is generating the proper employment options for skilled worker with high perks. On the other side banking and insurance sector help in providing the strength to the Indian economic condition and develop the foreign exchange system in country. So,it can be concluded that FDI always helps to create employment in the country, supports the small scale industries also and helps country to put an impression on the world wide level through liberalization and globalization.
- REETU SHARMA AND NIKITA KHURANAfinds that the growth of FDI gives opportunities to Indian industry for technological up gradation, gaining access to global managerial skills and practices, optimizing utilization of human and natural resources and competing internationally with higher efficiency. He added that FDI plays an important role in economic growth of an economy. Literature on factors determining FDI inflows into an economy shows that many factors influences inflows such as market size, inflation, trade openness, interest rate, wage rate, business environment, etc. His study examined the sector wise FDI inflows in India during post reform period. The results of their analysis show that FDI is related positively with real GDP and previous period FDI inflow but inversely related with inflation.
- DEVAJITconducted the study to find out the impact of foreign direct investments on Indian economy and concluded that Foreign Direct Investment (FDI) as a strategic component of investment is needed by India for its sustained economic growth and development through creation of jobs, expansion of existing manufacturing industries, short and long term project in the field of healthcare, education, research and development.
- KUMAR AND KARTHIKA found out in their study on "Sectoral Performance through Inflows of Foreign Direct Investment (FDI)", that Foreign Direct Investment has a major role to play in the economic development of the host country. Most of the countries have been making use of foreign investment and foreign technology to accelerate the place of their economic growth. FDI ensures a huge amount of domestic capital, production level and employment opportunities in the developing countries, which a major step towards the economic growth of the country.

3. Objectives and Research Methodology

Exploratory research is being conducted here. The data for the study is collected from secondary sources like research papers, journals, websites, newspapers. Taking into consideration the objectives of the study the research design employed for the study is of descriptive type. Graphs and tables have also been used where ever required to depict statistical data of FDI during the study period. Researcher used the Secondary data:

- Websites of Government and Journals related with FDI
- Books and magazines related to FDI inflows relate with different sectors
- Reports and publications of various associations connected with business and industry, Agencies, government etc.

The following are the objectives of the study:

- To understand the concept and need of FDI in India
- To study the sector wise role and year wise analysis of FDI .
- To study the trends of FDI in India.
- To know the flow of investment in India.
- To know the country wise country inflows in India.

4. Trends of FDI

This table clearly shows that, FDI inflow during the period 2000-01 to 2013-14. It has been increased from US $ 4029 Million to US $ 37745Millions in 2009-10 and in 2012-13 it was US $ 36860 Millions. During 2000-2001 to 2009-2010 ,total FDI was estimated as Rs.740117 Crores and in US $164551Millions. The inflow of FDI has been increased by 53.66 times. Table depicts that flows of FDI received in India during April 2000 to October 2013 i.e. 309,012 US$ million. From the year 2000 to 2002 FDI inflow in India has shown a increasing trend. This may be the result of Foreign Exchange Management Act (FEMA) which is introduced in 1999. Further it follow negative trend up to period 2003-2004. But from the year 2004-05 to 2008-09 investment into India once again start growing. The highest FDI inflows growth in the country in 2006-2007 year was 146%. Further, FDI inflows rose by 34 % to US$ 46,556 million during 2011-12. Last year April 2012-13 has shown negative growth rate i.e. -21% to US$ 36,860 million while the cumulative amount of FDI equity inflows from April 2000 to October 2013 stood at US$ 309,012 billion, according to the latest data released by the Department of Industrial Policy and Promotion (DIPP).

S. No.	Financial Year (April To March)	Total FDI flow in US$ Million	Total FDI Flows % Growth Over Previous
1.	2000-01	4,029	-
2.	2001-02	6,130	(+) 52 %
3.	2002-03	5,035	(-) 18 %
4.	2003-04	4,322	(-) 14 %
5.	2004-05	6,051	(+) 40 %
6.	2005-06	8,961	(+) 48 %
7.	2006-07	22,826	(+) 146 %
8.	2007-08	34,843	(+) 53 %
9.	2008-09	41,873	(+) 20 %
10.	2009-10	37,745	(-) 10 %
11.	2010-11	34,847	(-) 08 %
12.	2011-12	46,556	(+) 34 %
13.	2012-13	36,860	(-) 21%
14	2013-14(Apr-Oct, 2013)	18,934	-
Cumulative total (from april2000 toOctobeer2013)		309,012 -	-

Table 1: Financial Years 2000-01 to 2013-14 (up to November, 2013)
Source: DIPP, Federalministry of commerce and industry, govt. of India

A simple Growth Rate of FDI inflow for the period 2000-2014 has been calculated. Table examines that, the growth rate of FDI ranged between -18% to 146% and reached the highest point in the year 2006-2007 and the lowest point -18% in the year 2002-2003. The FDI trends have been come down because of the main impact of the global crisis during the year 2007-08.FDI growth rate remained negative in the year 2002-2004(-18%,-14%). The FDI inflow again showed increasing trend from 2004-2009. The FDI inflow show cyclical trends.

5. State -Wise FDI Inflow in India

In India there are 28 States and 7 Union Territories. All the states give top priority to attract FDI on a large scale for developmental purpose. FDI inflow to states varies widely which leads to concentration of FDI inflow. The top six states, viz., Maharashtra, New Delhi, Karnataka, Gujarat, Tamil Nadu and Andhra Pradesh accounted for over 70 per cent of the FDI equity flows to India between 2008-09 and 2011-12. The top two states, i.e., Maharashtra and Delhi accounted for over 50 per cent of FDI flows during this period. Maharashtra alone accounted for over 30 per cent of FDI flows to India during the same period.Despite impressive growth rates achieved by most of the Indian states as well as aggressive investment promotion policies pursued by various state governments, the concentration of FDI flows across a few Indian states continues to exist.

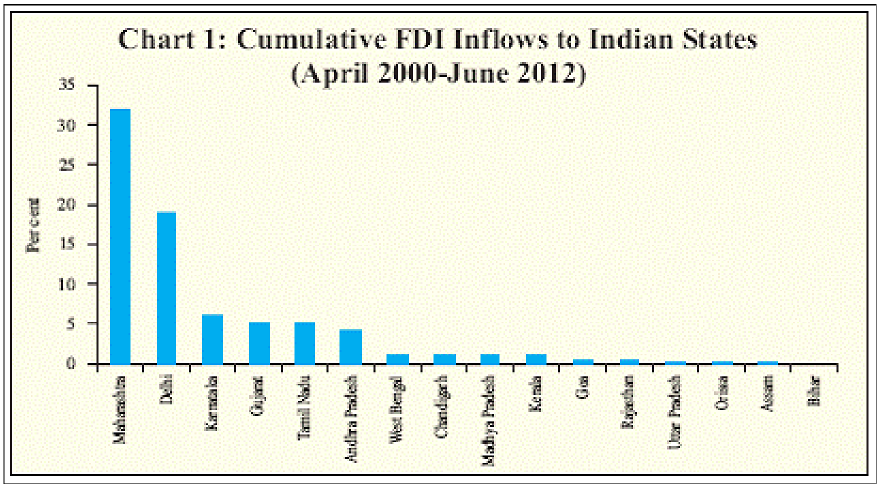

Figure 2
Source:http://www.rbi.org.in

States Delhi, Karnataka, Gujarat enjoyed second, third and fourth places in FDI attraction receiving 24.5%, 8%, 7% of total FDI respectively.Other States Tamil Nadu, Andhra, West Bengal, Chandigarh, Madhya Pradesh, Kerela attracted only 17% of FDI., Goa, Rajasthan, Bihar, Orissa and West Bengal attracted the lowest share of 4% State FDI Inflow in the year 2000-2010.The reason why some states are ahead of others in receiving FDI is because of favorable government responses, quick bureaucracy, good infrastructure facilities and rich heritage of entrepreneurship. Some states have locational disadvantage. FDI is uncovered due to poor infrastructure in big state like Bihar.

6. Sector-Wise FDI Flows in India

- FDI in Hotel & Tourism sector in India: 100% FDI is permissible in the sector on the automatic route. The term hotels include restaurants, beach resorts, and other tourist complexes providing accommodation and/or catering and food facilities to tourists. Tourism related industry include travel agencies, tour operating agencies and tourist transport operating agencies, units providing facilities for cultural, adventure and wild life experience to tourists, surface, air and water transport facilities to tourists, leisure, entertainment, amusement, sports, and health units for tourists and Convention/Seminar units and organizations.
- FDI in Power Sector in India: Up to 100% FDI allowed in respect of projects relating to electricity generation, transmission and distribution, other than atomic reactor power plants. There is no limit on the project cost and quantum of foreign direct investment.
- Drugs &Pharmaceuticals :FDI up to 100% is permitted on the automatic route for manufacture of drugs and pharmaceutical, provided the activity does not attract compulsory licensing or involve use of recombinant DNA technology, and specific cell / tissue targeted formulations.
- Non-Banking Financial Companies (NBFC): 49% FDI is allowed from all sources on the automatic route subject to guidelines issued from RBI from time to time.
- FDI in Insurance sector in India: FDI up to 26% in the Insurance sector is allowed on the automatic route subject to obtaining licence from Insurance Regulatory & Development Authority (IRDA)
- Roads, Highways, Ports : FDI up to 100% under automatic route is permitted in projects for construction and maintenance of roads, highways, vehicular bridges, toll roads, vehicular tunnels, ports.
- Pollution Control and Management : FDI up to 100% in both manufacture of pollution control equipment and consultancy for integration of pollution control systems is permitted on the automatic route.
- Call Centers in India : FDI up to 100% is allowed subject to certain conditions.
- Business Process Outsourcing in India: FDI up to 100% is allowed subject to certain conditions.
- Foreign Direct Investment in Small Scale Industries (SSI's) in India :Recently, India has allowed Foreign Direct Investment up to 100% in many manufacturing industries which were designated as Small Scale Industries.
- FDI in Telecommunication sector: In basic, cellular, value added services and global mobile personal communications by satellite, FDI is limited to 49% subject to licensing and security requirements and adherence by the companies (who are investing and the companies in which investment is being made) to the license conditions for foreign equity cap and lock- in period for transfer and addition of equity and other license provisions. a) ISPs with gateways, radio-paging and end-to-end bandwidth, FDI is permitted up to 74% with FDI, beyond 49% requiring Government approval. These services would be subject to licensing and security requirements.b) No equity cap is applicable to manufacturing activities.

S. No	Sectors	Amount of FDI Inflows (In US$ million)	%age with total FDI Inflows
1	Services Sector	38,713.32	18.55
2	Construction Development	22,969.45	11.00
3	Telecommunications	12,888.72	6.17
4	Computer Software & Hardwar	12,220.28	5.85
5	Drugs &Pharmaceuticals	11,570.50	5.54
6	Chemicals(OTHER THAN FERTILIZERS)	9,362.40	4.49
7	Automobile Industry	9,133.26	4.38
8	Power	8,357.23	4.00
9	Metallurgical Industries	7,780.61	3.73
10	Hotel & Tourism	6,825.56	3.27
11	Petroleum& Natural Gas	5,483.63	2.63
12	Food Processing Industries	5,230.08	2.51
13	Trading	4,236.54	2.03
14	Information & Broadcasting	3,639.93	1.74
15	Electrical Equipments	3,276.62	1.57

Table 2: Sector-Wise FDI Flows From April 2000 to July 2014
Source: DIPP, Federal Ministry of Commerce & Industry, Government of India

Table 2 clearly show the FDI inflows in different sector for the period April 2000 to Nov 2013 data reveals that most of the Foreign countries like to invest in service sector. The share of service sector was the highest i.e. 18.55% and their amount US $.38713.32 Millions .

7. Country Wise Equity FDI Inflows to India

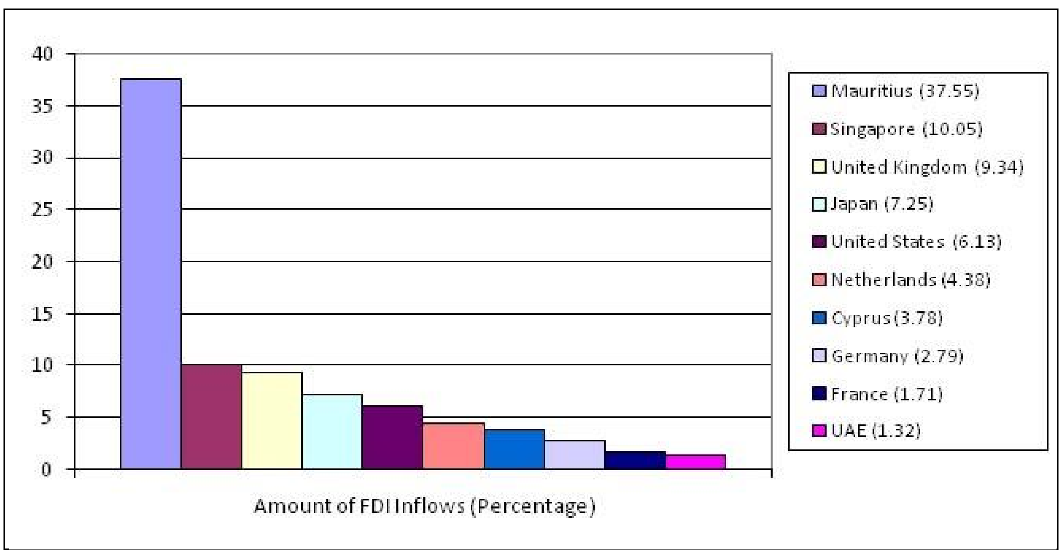

Figure 3
Source: DIPP, Federal Ministry of Commerce & Industry, Government of India

Chart depicts the country wise FDI inflow in India during April 2000 -Nov 2013. Mauritius emerged as the most dominant source of FDI contributing 77,083.47 US$ million and 37.55% of the total investment in the country. It is because the India has Double Taxation Avoidance Agreement(DTAA) with Mauritius . At second place is Singapore with 10 per cent of the FDI pie. The credit for the same can be given to loopholes in a Double Taxation Avoidance Agreement (DTAA) or Mauritius Treaty signed on April 1, 1983.

8. Conclusion
India’s Foreign Direct Investment (FDI) policy has been gradually 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. India has high potential to

attract FDI inflow. The present study found that total FDI inflow in India from April 2000 to November 2013 is 309,012 US$ million. The study also reveals that Mauritius emerged as the most dominant source of FDI contributing 77,083.47 US$ million of the total investment in the country. The services sector accounted for a steeply rising share of FDI stocks in India followed by construction development, Telecommunications and Computer Software & Hardwar. It can be observed from the above analysis that at the sectoral level of the Indian economy, FDI has helped to raise the output, productivity and employment in some sectors especially in service sector. Indian service sector is generating the proper employment options for skilled worker with high perks. On the other side banking and insurance sector help in providing the strength to the Indian economic condition and develop the foreign exchange system in country. So, we can conclude that FDI always helps to create employment in the country and also support the small scale industries also and helps country to put an impression on the world wide level through liberalization and globalization.

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