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Research Article

Effect of direct foreign investment in Indian national economy

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SUMMARY : Foreign direct investment (FDI) as a strategic component of investment is needed by India for achieving the economic reforms and maintains the pace of growth and development of the economy. The paces of FDI in lows in India initially were low due to regulatory policy framework but there is a sharp rise in investment flows from 2005 towards because of the new policy has broadened. The study tries to find out how FDI seen as an important economic catalyst of Indian economic growth by stimulating domestic investment, increasing human capital formation and by facilitating the technology transfers. The main purpose of the study is to investigate the impact of FDI on economic growth in India.

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BACKGROUND AND OBJECTIVES

Foreign direct investment (FDI) refers to the net inflows of investment to acquire a lasting management interest (10 per cent or more of voting stock) in an enterprise operating in an economy other than that of the investor.

There are two types of FDI: inward foreign direct investment and outward foreign direct investment, resulting in a net FDI inflow (positive or negative) and "stock of foreign direct investment", which is the cumulative number for a given period. Direct investment excludes investment through purchase of shares. FDI is one example of international factor movements. Foreign Direct Investment (FDI) is fund flow between the countries in the form of inflow or outflow by which one can able to gain some benefit from their investment whereas another can exploit the opportunity to enhance the productivity and find out better position through performance. The effectiveness and efficiency depends upon the investors perception, if investment with the purpose of long term then it is contributes positively towards economy on the other hand if it is for short term for the purpose of making profit then it may be less significant. The FDI may also affect due to the government trade barriers and policies for the foreign investments and leads to less or more effective towards contribution in economy as well as GDP of the economy.

RESOURCES AND METHODS

Government of India has set up Foreign Investment Promotion Board (FIPB) for processing of FDI proposals in India. The Board is the apex inter-ministerial body of the Central Government that deals with proposals relating to FDI into India for projects or sectors that do not qualify for automatic approval by the Reserve Bank of India (RBI) or are outside the parameters of the existing FDI policy.

Importance of the study:

The study attempts to analyze the important dimensions of FDI in India. The study works out on the pattern and trends of the main determinants and dimensions of investment flow in India. The study also examines the role of FDI on economic growth in India for the period 1991 – 2011. The period of study is important because:

- July, 1991, India opened is doors to private sector and liberalized it economy.
- Experience of South – East Asian countries by liberalizing their economies in 1980s became stars of the economic growth and development in 1990s.
- India experience with its first generation economic reform and the country's economic growth and performance were considered safe heavens for FDI which led to second generation of economic reform in India in first decade of century.
- There is a considerable change in the attitude of both developing and developed countries towards FDI.
- They both considered FDI as most suitable form of external finance.
- Increase in competition for FDI inflows particularly among developing nations.
- Current issues related to FDI in retail sector (Multi brand retail).

Data collection:

The study is based on secondary data. The required data were collected from various sources *i.e.* World Investment Reports, Asian Development Bank's Reports, various bulletins of Reserve Bank of India, publications from Ministry of Commerce, Govt. of India that were available on internet. It is a time series data and relevant data have been collected for the period of 1991 – 2011.

OBSERVATIONS AND ANALYSIS

Government of India has decided to allow 26 per cent FDI and 23 per cent FII investment in commodity exchange, subject to the provision that no single entity will hold more than 5 per cent stake.

It could be observed that there has been a steady build up in the actual FDI inflows in the pre-liberalization period in Table 1. But measures introduced by the government to liberalize provisions relating to FDI in 1991 increased FDI Rs. 2705 corers in 2010. The list of investing countries to India reached to 150 in 2010 as compared to 29 countries in 1991. Never less, still a lion's share of FDI comes from only a few countries.

Table 2 showed the actual investment flows of top ten countries during the period of 2008-09 to 2010-11. The FDI stock for this period from Mauritius was the largest (42%). The other top nine countries are Singapore, USA, UK, Netherlands, Japan, Cyprus, Germany, France and UAE. It implies that these top ten countries accounted for well over 78 per cent of the FDI inflows during the above period. The Mauritius which was not in the picture till 1992 has the highest growth rate because such investment is represented by the holding companies of Mauritius set up by the US firms. The reason behind the US companies have routed through Mauritius is the tax treaty between Mauritius and India stipulates a dividend tax of five percent while the treaty between India and US stipulated a dividend tax of 15 per cent.

Although India's share in global FDI has increased considerably, but the pace of FDI inflows has been slower than China, Singapore, Brazil and Russia.

Table 1: FDI inflows in India (from 1948-2010)

Amount of FDI	Mid 1948	March 1964	March 1974	March 1980	March 1990	March 2000	March 2010
In corers	256	565.5	916	933.2	2705	18486	123378

Table 2 : Share of top ten investing countries in FDI inflows (Financial year wise)

Ranks	Country	2008-09 (April-March)	2009-10 (April-March)	2010-11 (April-March)	Cumulative inflows (from Apr-2000 to March- 2011)	Percent of total Inflow in Rupees)
1	Mauritius	508993.1	496333.7	318547.8	2427607.2	42
2	Singapore	157266.7	112948.2	77296.6	528762.9	9
3	USA	80017.8	92304.3	53526.7	425422.4	7
4	UK	38404.1	30941.5	34342	294326.8	5
5	Netherlands	39215	428226.7	55012.3	256268.9	4
6	Japan	18885.6	56704	70629.8	239579.2	4
7	Cyprus	59828.3	77275.8	41706.7	219479.4	4
8	Germany	27497.3	29800.4	9078.8	133761.8	2
9	France	20980.5	14368.3	33486.3	102673.1	1
10	UAE	11333.3	30168.2	15691.8	85921.8	--
Total	FDI inflows	1230248.8	1231196.4	885193.7	5807223.3	--

Due to continued economic liberalization since 1991, India has seen a decade of 7 plus per cent of economic growth. In fact, India's economy has been growing more than 9 per cent for three consecutive years since 2007 which make country make a proficient performer among global economies.

At present India is the 4th largest and 2nd fastest growing economy in the world. It is the 11th largest economy in terms of industrial output and has the 3rd largest pool of scientific and technical manpower.

There has been a generous flow of FDI in India since 1991 and its overall direction also reminded the same over the years irrespective of the ruling party. India has considerably decreased its fiscal deficit form 4.3 per cent in 2002-03 to 2.7 per cent in 2007- 08 and 1.15 in year 2009-11.

FDI plays a crucial role in enhancing the economic growth and development of the country. Moreover, FDI as a strategic component of investment is needed by India for achieving the objectives of its second generation of economic reforms and maintaining the pace of growth and development of the economy. Similarly Dua and Rashid (1998) studied FDI and economic activity in India.

Conclusion:

Government should design the FDI policy such a way where FDI inflow can be utilized as means of enhancing domestic production, savings and exports through the equitable distribution among states by providing much freedom to states, so that they can attract FDI inflows at their own level. FDI for further opening up of the Indian economy, it is advisable to open up the export oriented sectors and higher growth of the economy could be achieved through the growth of these sectors.

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