Vol 4 Issue 7 Jan 2015 ISSN No :2231-5063

International Multidisciplinary Research Journal

Golden Research Thoughts

Welcome to GRT

RNI MAHMUL/2011/38595 **ISSN No.2231-5063**

Golden Research Thoughts Journal is a multidisciplinary research journal, published monthly in English, Hindi & Marathi Language. All research papers submitted to the journal will be double - blind peer reviewed referred by members of the editorial board.Readers will include investigator in universities, research institutes government and industry with research interest in the general subjects.

International Advisory Board

Editorial Board

Address:-Ashok Yakkaldevi 258/34, Raviwar Peth, Solapur - 413 005 Maharashtra, India
Cell : 9595 359 435, Ph No: 02172372010 Email: ayisrj@yahoo.in Website: www.aygrt.isrj.org

Golden Research Thoughts
ISSN 2231-5063
Impact Factor : 3.4052(UIF)
Volume-4 | Issue-7 | Jan-2015
Available online at www.aygrt.isrj.org

GRT

FOREIGN DIRECT INVESTMENT PROSPECTIVE & CHALLENGES

Mutturaj N B

Assistant Professor, Dept. of Commerce , G F G College, Kamalapur , Gulbarga, Karnataka.

Abstract:- Foreign Investment in India has been the direct outcome of the liberal trade policies undertaken and implemented by successive governments. The liberalization program of the government aims at rapid and substantial growth of the country's economy and besides a harmonious integration with global economy. While foreign investment in India comprises of investments made by overseas companies in India, the reverse i.e. outflow of foreign investment from India is also prevalent in the Indian economy. Foreign investment in India has created some wonderful opportunities in the country in terms of creating employment and improving the basic infrastructure of the country.

Keywords: Policies, Foreign Investment Employment Economics, prevalent.

INTRODUCTION

India is among one of the few markets in the world that offers such high prospects of growth and earning in virtually all sectors of the economy. The huge skilled workforce is one factor that ensures that foreign investors get a good return on their investments.

This study takes a closer look at the structure of Foreign Direct Investments inflows and outflows from India. It traces the development of India's economic policy regard FDI and the resulting changes in both inflows and outflows. The expansion of FDI into and from India has been accompanied by a rapid economic growth and an increasing openness to the rest of the world.

Foreign Investment in India has huge potentials. However, foreign investment in India has its own share of advantages and disadvantages. Overseas investors must prepare themselves well in advance to face with adversities and deal with them properly. Some of the drawbacks that investors may have to face are bureaucratic hassles, infrastructural deficiencies, power shortages and sometimes political uncertainty. Despite these uncertainties, India presents a huge potential to global players to invest in the market. Many leading overseas brands have already invested while some of the companies have plans in the pipeline to invest in India.

FOREIGN DIRECT INVESTMENT: PROCPECTIVES AND CHALLENGES

Perceptions and polices with regard to the role of foreign capital in the process of industrial and overall growth have changed in India since the beginning of economic planning. The Government of India saw in FDI a potential, non-debt creating source of finance and a bundle of assets , viz., capital, technology, market access, employment, skills, management techniques, and environment, which could solve the problems of low income growth , shortfall in savings, investments and exports, and unemployment.

Foreign direct investment (FDI) is no longer an activity exclusively undertaken by firms from developed countries. The growth of multinational enterprises (MNEs) from emerging markets has begun to focus attention around the world on the role these new players. The rise of outward investment from emerging markets has contributed to the growth in FDI globally. In 1980, global FDI outflows totaled US$52 trillion, and emerging markets accounted for only 6% of this figure. By 2007, global FDI outflows approached US$2 trillion, and emerging markets accounted for over 15% (or US$300 billion) of the total, India is today one of the most favored investment destinations in the world ,ranked as the world's third best FDI destination after China and the USA, in 2003, India ranked sixth on the list. The Goldman Sachs Global Economic Paper of Oct 2003 =dreaming with BRICS : the path to 2050'had predicted that over the next 50 years, Brazil, Russia, India and China and the USA could become a much larger force in the world economy. India has declared that, ? now it is destination India unlike China in the past? . Several steps have been initiated recently to facilitate increased FDI inflows.

FOREIGN INVESTMENT POLICY IN INDIA

The policy of the government of India towards the foreign direct investment has been positive due to the shortage of domestic capital. This is evident from various industrial policy resolutions and the declarations issued by the government from time to time. However, foreign investors did not show keen interest in investing in India until 1991 due to the type of economic system of our country. The economic liberalizations of 1991 have given greater fillip to the foreign direct investment. The Government of India with regard to FDI has undertaken various liberal policy decisions to make the whole process of foreign investment in India hassle free. Some of the foreign investment policies include:

1.The list of industries that are eligible for automatic approval of foreign investment has been expanded by the Ministry of industry.
2.The upper limit of the rate of foreign investment in India has been raised to 74% from the earlier 51%; in some cases this has been increased to 100%.
3.Indian companies will no longer need prior clearance from the reserve Bank of India, RBI for inward remittance of foreign exchange or for issuing of shares to foreign investors.
4.The exchange control regulations have been amended by the government.
5.The ban against the use of foreign brand names/trademarks has been removed.
6.The corporate rate of corporate tax on foreign companies has been reduced from 65% to 55% by the government in the annual budget of 1994-95.
7.The government reduced long term capital gains rate for overseas companies to 20%.
8.Under the Indian Income Tax Act, export earnings are exempted from corporate income tax for both overseas and domestic firms.
9.100% inflow of foreign investment is permitted in strategic sectors such as roads, ports, tunnels, highways and harbors on the condition that the total investment in any of the sector should not exceed Rs.1500 corer.
10.Any increase within the prescribed limit does not require permission from the foreign investment promotion board.

INFLOW OF FDI INTO INDIA

Table1: FINANCIAL YEAR-WISE FDI INFLOWS DATA:
(Data on FDI have been revised since 2000-01 with expended coverage to approach International Best Practices)

(Amount US$ million)

FOREIGN DIRECT INVESTMENT (FDI)								
S.No.	Financial Year	EQUITY		Reinvested earnings +	Other capital +	FDI FLOWS INTO INDIA		Investment by FII's Intuitional investors fund (net)
		FIPB Route/ RBI's Automatic Route/ Acquisition Route	Equity capital of unincorn-orated bodies#			Total FDI Flows	% growth over previous year(in US $ terms)	
1	2000-01	2339	61	1350	279	4029	-	1847
2	2001-02	3904	191	1645	390	6130	(+)52 %	1505
3	2002-03	2574	190	1833	438	5035	(-) 18 %	377
4	2003-04	2197	32	1460	633	4322	(-) 14 %	10918
5	2004-05	3250	528	1904	369	6051	(+) 40%	8686
6	2005-06	5540	435	2760	226	8961	(+) 48%	9926
7	2006-07	15585	896	5828	517	22826	(+)146 %	3225
8	2007-08	24573	2291	7679	292	34835	(+) 53%	20328
9	2008-09	27329	702	9030	777	37838	(+) 09%	(-)15017
10	2009-10 (P) (+)	25609	1540	8669	1931	37763	(-) 10 %	29048
11	2010-11(P)(+)	21376	874	11939	658	34847	(-) 08%	29422
12	2011-12 (P)	34833	1021	8205	2494	46553	(+) 34%	16813
13	2012-13 (P)	16348	786	8217	1846	27197	-	16043
CUMULATIVE TOTAL (from Apr 2000 to Dec 2012		189489	9547	70518	10858	280412	-	133121

SOURCE:

i. RBI?s Bulletin February, 2013 dt. 11.02.2013 (Table No. 34 – FOREIGN INVESTMENT INFLOWS).
ii.Inflows under the acquisition of shares in March, 2011, August, 2011 & October, 2011, include net FDI on account of transfer of participating interest from Reliance Industries Ltd. to BP Exploration (Alpha).
iii.RBI had included Swap of Shares of US$ 3.1 billion under equity components during December 2006.
iv.Monthly data on components of FDI as per expended coverage are not available. These data, therefore, are not comparable with FDI data for previous years.
v.Figures updated by RBI up to December, 2012.
"#" Figures for equity capital of unincorporated bodies for 2010-11 are estimates.
(P) All figures are provisional
"+" Data in respect of „Re-invested earnings? & „Other capital? for the years 2009- 10, 2010-11 & 2012-13 are estimated as average of previous two years.

Table 1 presents the FDI inflows into India. The total capital inflows in India have increased from US $4029 million in 2001-02 to US $46553 million in 20010-11, which means that the, they have increased by about near 12 times in last 12 years. It has been observed that total FDI excluding portfolio investment i.e investment by FII's constitute a large part of capital flows and increasing year after year except 2002–04. At the same time, it is to be noted that the share of FII's has varied in a wide range and quite volatile from one year to another.

FOREIGN INVESTMENT BY INDIAN COMPANY

Until 1991, Indian companies made very little investment abroad. Although government of Indians policy had been one of encouraging foreign investment by India companies, subject to certain conditions, several factor like the domestic economic policy and the domestic economic situation were deterrents to foreign investment by Indian companies.

By restricting the areas of operation and growth, the government policy seriously constrained the potential of Indian companies to make a foray into the foreign countries through investment. Added to this was the attraction of the protected domestic market which was, in many cases, a seller's market and this made the India companies ignore the foreign markets. Indians companies have established subsidiaries and joint ventures in a number of countries in different manufacturing industries and service sectors. The liberalization, both global and domestic, has imparted a global orientation to Indian business so there has been a substantial increase in India investment abroad. FDI outflow from India crossed $ 13 billion in 2007 compared to the annual average of $ 121 million during 1990-2000. An UNCTAD report observes that India also stands out among Asian investors, not so much because of its recent and significant increase in outward FDI and because of its potential to be a large outward investor, but because of the new trend set by some of its information technology (IT) firms. Most Indian outward FDI is manufacturing (about 55 per cent), but non-financial services also account for a significant share (25 per cent). FDI in It services in particular has begun to grow rapidly. The growing technological capabilities of India firms and rising exports, particularly in IT service and pharmaceuticals, are driving the FDI growth. Access to markets, distribution networks, foreign technology and strategic assets such as brand names, are the main motivations. Securing natural resources is also becoming an important driver for FDI in the oil and gas industries and mining.

The most important destination for India FDI has been the United States, accounting for nearly one-fifth of its total outward flows since the mid -1990s to 2003, followed by the Russians Federation (with 18 per cent) mainly due to acquisitions in the oil and gas industries. Overall, however, about half of total India outward FDI has gone to other developing countries. Strategic M&As have been finding favour with corporate India too. M&As by Indian companies involving foreign firms fall into three categories, viz., acquisition of foreign firms, acquisition of MNC affiliates in India and acquisition of foreign brands. Foreign investment, both in Greenfield enterprises and mergers and acquisitions (M&A), is clearly a part of the globalization strategy of many India companies. Recently, there has been a spurt in FDI by India companies. In light of the economic liberalization and the growing competition at home, many India companies have been planning for a major thrust abroad.

PROSPECTIVE OF FDI

Foreign Direct Investment plays a pivotal role in the development of India's economy. It is an integral part of the global economic system. Advantages of FDI can be enjoyed to full extent through various national policies and international investment architecture. Both the factors contribute enormously to the maximum FDI inflows in India, which stimulates the economic development of the country. Some of the biggest advantages of FDI enjoyed by India have been listed as under:

Economic growth- This is one of the major sectors, which is enormously benefited from foreign direct investment. A remarkable inflow of FDI in various industrial units in India has boosted the economic life of country.

Trade- Foreign Direct Investments have opened a wide spectrum of opportunities in the trading of goods and services in India both in terms of import and export production. Products of superior quality are manufactured by various industries in India due to greater amount of FDI inflows in the country.

Employment and skill levels- FDI has also ensured a number of employment opportunities by aiding the setting up of industrial units in various corners of India.

Technology diffusion and knowledge transfer- FDI apparently helps in the outsourcing of knowledge from India especially in the Information Technology sector. It helps in developing the know-how process in India in terms of enhancing the technological advancement in India.

Linkages and spillover to domestic firms- Various foreign firms are now occupying a position in the Indian market through Joint Ventures and collaboration concerns. The maximum amount of the profits gained by the foreign firms through these joint ventures is spent on the Indian market.

CHALLENGES FOR FDI

Foreign capital, both private and official (government and institutional), have certain limitations. Certain additional risks are associated with the foreign capital. One of the important limitations to utilize the foreign capital is the absorptive capacity of the recipient country, i.e., the capacity of the country to utilize the foreign capital effectively .Lack of infrastructural facilities, technical know-how, personal, inputs, market, feasible projects, inefficiency or inadequacy of administrative machinery etc. are important factors that affect the absorptive capacity.

Sometimes strings' are attached to the official assistance the recipient country may be pressurized to fall in line with the ideology or direction of the donor. The following criticisms are leveled against foreign capital:

• Private foreign capital tends to flow to the high profit areas rather than to the priority sectors.
• The technologies brought in by the foreign investor may not be adapted to the consumption needs size of the domestic market resource availabilities stage of development of the economy etc.
• Through their power and flexibility the multinational corporations can evade or undermine economic autonomy and control, and their activities may be inimical to the national interests of particular countries.
• Foreign investments sometimes have unfavorable effect on the balance of payments of a country because the drain of foreign by way of royalty, dividend, etc. is more than the investment made by the foreign concern.
• Foreign capital sometimes interferes politics.
• Foreign investors sometimes engage in unfair and unethical trade practices.
• Sometimes foreign investment can result in the dangerous situation of minimizing/ eliminating competition and the creation of monopolies or oligopolistic structures.
• FDI can also potentially displace domestic producers by pre-empting their investment opportunities.
• Often, several costs are associated with encouraging foreign investment. Meier observes5 that these costs may arise from special concessions offered by the host country, adverse effects on domestic saving deterioration in the terms of trade and problems of balance of payments adjustment.

CONCLUSION

Removing its long held restrictive foreign investment policy in 1991, India sought to compete with the successful Asian economics to get a greater share of world‘s FDI. Ongoing initiatives, such as further simplification of rules and regulations, improvement in infrastructure are expected to provide necessary impetus to increase FDI inflows in future. The inflows of FDI would depend on domestic economic conditions, world economic trends, and strategies of global investors. Government, on its part, is fully committed to creating strong economic fundamentals and an increasingly proactive FDI policy regime.

Moreover, various government and non-governmental organization‘s report revealed India‘s potentiality as a FDI destination in developing countries next to china, but performance is still very poor. The prospects of India as a FDI destination would be realize if some of its constrains could be overcome.

Although FDI inflows to India has been increasing, regional distribution of the same is found to be more inequitable. To ensure a more equitable regional distribution of such flows, both central and state government should take concerted strategy for improvement in infrastructure facilities and creation of sound economic and political environment. Development of infrastructure, especially power and transport network is an immediate need of the time, since it is basic for industrialization. Bureaucratic hassles, corruption and time consuming procedure should be reduced to attract more FDI inflow. After all, a more transparent investment system will benefit and secure future prospect of FDI inflow in India.

REFERENCES:

1.Department of Industrial Policy and Promotion, 2010. "Foreign Direct Investment (FDI) in MultiBrand Retail Trading," Discussion paper. Available at http://www.dipp.nic.in.
2.Dube, Arindrajit, Lester, T. William and Eidlin, Barry, 2007. "Firm Entry and Wages: Impact of WalMart Growth on Earnings Throughout the Retail Sector." Available at http://ssrn.com/abstract=841684.
3.Hausman, Jerry A. and Ephraim Leibtag, 2004. "CPI Bias from Supercenters: Does the BLS Know that Wal-Mart Exists?" NBER Working Paper No. w10712.
4.Hausman, Jerry A. and Ephraim Leibtag, 2007. "Consumer Benefits from Increased Competition in Shopping Outlets: Measuring the effect of Wal-Mart."Journal of Applied Econometrics, Vol. 22, No. 7, pp. 1157–1177.
5.Head, Keith, Ran Jing, and Deborah L. Swenson, 2010. "From Beijing to Bentonville: Do Multinational Retailers Link Markets? NBER Working Paper No. 16288.

Mutturaj N B
Assistant Professor, Dept. of Commerce , G F G College, Kamalapur , Gulbarga, Karnataka.