CHAPTER - 2
REVIEW OF LITERATURE

Foreign Direct Investment has become a necessary engine of growth in developing countries that are scarce with resources. FDI contributes to international trade integration, technology spillovers, assists human capital formation, helps create a more competitive business environment and enhances enterprise development, which is the most potent tool for alleviating poverty in developing countries. As per Blomstrom (1990), Multi National Enterprises (MNEs) are likely to bring in the host country capital, technology and knowledge and potentially lead to increased exports, boosting international comitiveness. FDI therefore contributes to overall economic development surging through its various channels (Seethapathi K, 2006).

Various literatures available define FDI in various ways Yasheng Huang (2003) defined FDI as a financial stake a foreign company acquires in a domestic company. To qualify as FDI as per rules in China, the financial stake must be at least 25%. According to the definition given by IMF and OECD (2000), FDI is defined as an investment made by an investor of one country to acquire an asset in another country with the intent to manage that asset.

The Present Review of Literature on Foreign Direct Investment is broadly classified into

i. Studies on FDI in general

ii. Studies on the impact of FDI
2.1 STUDIES ON FDI IN GENERAL:

Lucas (1990) has analyzed the issue by examining the question of why capital does not flow from rich to poor countries and critically explored some answers that are based on human capital and capital market imperfections. With regard to human capital, he reveals that the rich country’s optimal policy is to retard capital flows so as to maintain real wages at artificially low levels in the poor country. As far as capital market imperfections are concerned, Lucas’s paper analyzes a borrowing contract between poor and rich countries. In this paper, the focus is on linkages and on the rational behavior of different foreign investors, in the face of reform uncertainty.

Kumar and Siddharthan (1994) analyzed the inter-firm variation in export behaviour in 132 Indian manufacturing industries using panel data for 640 firms for the period 1987-88 to 1989-90. It was argued that the technology factor could be important for explaining the export performance of Indian enterprises in case of low and medium technology industries. The same was empirically verified by conducting a framework of Tobit models in view of the fact that a large number of Indian enterprises did not export and hence the dependent variable had a zero value in many cases. It was examined in particular the role of firm size, in-house innovation and technology imports, relative advertising and capital intensity of operations controlling affiliation with multinational enterprises and export incentives and concessions offered by the Indian government. The results had proved the prediction that in developing countries such as India, a firm’s technological activity favorably
influenced its export behavior only in medium and low technology industries. MNE affiliates in general did not exhibit a significantly different export behavior from other firms. It was found that in economies with large protected markets as in India, local firms tend to focus on the domestic market.

Singh Harjit (1995) in his study made an attempt to explain the Foreign Direct Investment (FDI) activity of multinational enterprises (MNE). This study extended the eclectic perspective by adopting an integrated framework to explain how the MNE’s strategic planning process influenced the FDI performance. In this study a survey of 96 U.S. companies that have recently invested abroad in 37 countries have been conducted. This study reveals that the strategic planning process of MNE’s has a major impact on the success of their FDI’s. The FDI-level analysis shows that firms also have to face integration and responsiveness pressures simultaneously.

Frederick W. Dow (1995) in his work made an attempt to compare US, Japan and European multinational enterprises in the degree to which their executives perceive financial, political, labor force, economic and strategic motive factors as motivating power for investment in Indonesia. A descriptive correlation method was employed in this study. A structured questionnaire was distributed to 474 U.S, Japanese and European multinational companies. Rank-ordering analysis, Kendall’s coefficient of concordance, ANOVA, Pearson’s correlation and Students’t-tests were used to analyze the data collected from 56 respondents. The study shows varied results between the perceiveness of executives in
U.S., Japan and European MNE’s. Finally, the study reveals that six significant mean differences exist between US, Japan and European executives of manufacturing and non-manufacturing firms in terms of motivating power of all financial, political, labor force, economic and strategic motive factors affected the decision to invest in Indonesia.

Anand and Delios (1996) documented that the relatively slow growth of FDI from Japanese MNCs in India as compared to China is attributed to the desire to gain only market access in India.

Garg, et al. (1996) documented that since 1986 along with the regulation of product prices, the Indian government has limited the profits the pharmaceutical firms could earn to around 6 percent of turnover. From 1970 to the early 1990s, industry pre-tax profitability as a percent of turnover declined. But during 1977-1978 industry profitability was around 12%. In 1982-1983, it declined to 7.5%, further declining to 3.5% during 1987-1988. Since 1992, industry profitability is rising, and by the year 1996 it reached nearly 10 percent of the turnover.

Magnus Blomstrom and Ari Kokko (1996) in their work made an attempt to review the empirical evidence on host country effects of Foreign Direct Investment. The study also examines the impact of foreign MNCs for the trade performance of their host countries and the effects on competition and industry structure in the host countries. The study concludes that MNCs play an important role for productivity and export growth in their host countries and impact of FDI varies from industry to industry, depending upon the characteristics and the policy environment prevailing in the respective countries.
Surendra Pradhan (2000) in his study made an attempt to examine the various aspects of FDI from investing firm and as well as from receiving firms’ point of view. This study mainly focuses on the risk and return from firms’ perspective and also the strategies that attract FDI from host countries point of view. The methodology used in this study for data analysis is based on Brown and Warner. An examination of shareholders responses to the announcement of FDI in emerging markets shows positive response which is indicated by higher risk adjusted rate of returns than expected on investments during the period surrounding the announcements. The higher rate of returns is in fact, the result of existing market opportunities combined with the host country’s policies towards FDI.

William Milberg (2000) in his work made an attempt to provide a critical survey of the debate over the net benefits of IFDI (inward Foreign Direct Investment) as a toll for economic development through raising employment and wages, generating technology spillover that raise productivity, providing export market access and leading to improvement in the balance of payments. The study shows that the hypothesized positive “technology spillover” effects of IFDI are difficult to verify empirically. The study reveals that IFDI has contributed to growing wage inequality in some developing countries, more than offsetting equalizing host country balance of payments.

Anusuya Yograrajah, Naresh Khatri and Zafar Uden (2000) in their work made an attempt to look at the impact of liberalization on Foreign Direct Investment in India. This study covers pre-1991 and post-1991
industrial policies of FDI in India and motivating factors for FDI in India. The study reveals that the industrial policies of the govt. of Indian are responsible for attracting FDI. The investment is made mostly in core sectors such as infrastructure, power and coal. The study also reveals that the low cost of labor and materials and the availability of market and infrastructure are likely to be the main factors attracting FDI in India.

Feinberg & Majumdar (2001) found that Liberalisation of FDI policies offers opportunities for firms as well as threats. If FDI (and trade) liberalisation results in faster growing national economies, then firms face larger, faster-growing markets domestically.

Henry F.L. Chung and Peter Enderwick (2001) in their study made an attempt to examine the key factors such as international business, immigrant effect, service requirements and market size as important determinants of the choice between exporting and Foreign Direct Investment. This study employed a logistic regression analysis method to examine the market entry mode decisions of 124 New Zealand firms operating in a single foreign market (Taiwan). The analysis of the study reveals that significant factors identified included product type and proxy experience (firms’ experience with Japan) and an “immigrant effect” which impacted on the choice of FDI mode.

The Ministry of Commerce and Industry, Government of India (2002), in consultation with the RBI, had constituted a committee in May 2002 to look into the methodology and compilation of FDI issues in an effort to bring the reporting system of FDI data in India into alignment with international best practices. The committee had recommended that the
FDI statistics should include, besides equity capital, ‘reinvested earnings’ (retained earnings of FDI companies) and ‘other direct capital’ (inter-corporate debt transactions between related entities) in accordance with the international best practices.

Nagraj R (2003) in his study documents the trends in Foreign Direct Investment in India in the 1990s and compares them with those of China. This study also raises some issues on the effect of the recent investment on the domestic economy. Based on the analytical discussion and comparative experience, the study reveals that about 40-50 percent of China’s FDI represents its domestic survey and another 25% represents real estate by Overseas Chinese. The quantum of foreign investment from the advanced economies that could improve domestic production is not so different from that in India, in relation to its domestic output. The China’s foreign investment regime is said to be more restrictive than India’s. The study concludes that India should be concerned about is not so much the absolute quantum of the inflows, but how effectively it uses its external openness to augment the domestic capability and access foreign markets.

Sebastian Morris (2004) in his work made an attempt to study the regional determinants of FDI in India and Gujarat. The study specifically uses Stephen Flymers’ understanding of the parallels and relationship between the international organization of a global firm and the locational choices for the same with spatial aspects of the location of economic activities in general. The results from the study reveal that though Gujarat is not having large and metropolitan cities, the FDI in Gujarat
increased over the period when the state grew rapidly in the first six years from the post-liberalization period and after that the slow down of growth has been a retardant to FDI.

Alka Chadha (2006) in his study made an attempt to study the drugs and pharmaceutical sector that have had a very significant position in the Indian economy due to its positive technological spillovers. The study reveals that there has been a significant increase in FDI inflows after the year 1999. It is also found that despite the proven comparative advantage, The Indian Pharmaceutical exports contribute a negligible share to world pharmaceutical exports around 1% of total world pharmaceutical exports. In this study, it is concluded that the pharmaceutical industry is in the transition phase ready to face new challenges that could bring major changes in its business environment and for long term solutions, the industry should build up R&D facilities as well as make sustained efforts to attract FDI for technical collaborations.

Andrea Elliott and Kishore G Kulkarni (2006) in their study made an attempt to explore the factors that make FDI more attractive for foreign firms in the context of Nepal. The study also discusses the role played by FDI in the economic development of Nepal. The results from the study reveal that increased volume of FDI inflows is not very significant for the growth of Nepalese Gross Domestic Product (GDP) in both absolute as well as relative sense.
Srujan A (2006) in his study made an attempt to study the global, regional and country wise trends in Foreign Direct Investment. In this study a comparison of FDI in the developed and developing economies have been observed for the year 2000 to 2003. The study also covers the data relating to top 10 recipients of FDI inflows and sources of FDI inflows country wise belonging to Asia-Pacific and African regions. The study shows positive trends in the global FDI flows in respect to both FDI inflows and FDI outflows. The study also reveals that the FDI flows in different regions and countries depend upon the factors like global economic trends, liberalization activities and stock market movements and the elimination of hurdles such as political instability, issues in corporate governance, terrorism risk etc. create conducive atmosphere for higher FDI flows.

Sonam Jigme (2006) in his work made an attempt to study the factors affecting Foreign Direct Investment in Bhutan and also the potentials for increasing the volume of FDI in Bhutan. The results from the study reveal that there is no universal perception for attracting higher inflow of FDI into the country. The study further reveals that, in spite of limited resources, weak infrastructure, small market size and small population, Bhutan is committed to integrating into the world economy and enjoys benefits of integration by joining the global race to attract Foreign Direct Investment.

Tanay Kumar Nandi and Ritankar Saher (2007) in their work made an attempt to study FDI In India with a special focus on Retail trade. This paper emphases the need of FDI in India in retail sector and reveals
that the effects of FDI on the retail trade have been positive without harming the domestic economy. The study also suggests that FDI in retail sector must be allowed.

Chalapat Rao K.S., Ranganathan VK and Murthy M.R. (2007), in their work made an attempt to study the policies and procedures related to actual FDI inflows in selected sectors in India. The study reveals that information technology, transport equipment and other engineering industries, food processing sector and drug and pharmaceuticals offer a mix of export potential, technology intensity and employment generation and also accounted for a significant portion of FDI inflows into India in the new policy period.

Kalberine Connor Linton and Nicholas Carado (July 2007), in their study made an attempt to trace the impact of India’s changing patent laws on Foreign Direct Investment (FDI) in the pharmaceutical sector. The study is conducted to analyze the impact of law on domestic and foreign pharmaceutical investment. The study reveals that the multinational pharmaceutical firms have responded to the Indian movement towards TRIPS compliance by increasing the quantity and quality of FDI in the areas of R&D and manufacturing because of their more cautious attitude towards patenting and commercialization of pharmaceutical products in India.

Jaya Gupta (2008) in this study made an attempt to study the policy regime of liberalized India since 1991 with respect to both inward and outward Foreign Direct Investment (FDI). The study reveals that facts that FDI was permitted in almost all manufacturing industries except six
specified industries of strategic concern to the state. Under the new policy, FDI was also permitted in hotel and tourism industry and trading companies engaged in exports in the service sector. Insurance, defence, print media and now retail are the latest addition to the list of sectors that are open for foreign investments.

Ramesh kumar S and Alagappan V (2008) in their work made an attempt to examine the trends and patterns in Foreign Direct Investment (FDI) inflows in India during the post-liberalization period. The analysis of the study reveals that the actual FDI inflow into the country had maintained a fluctuating and inconsistent trend during the study period. The study also finds that the approvals for FDI inflows had been very slow in materializing themselves into actual inflows.

Recep Kok, Berner Arikgoz Ersoy (2009) in their study investigated the determinants of Foreign Direct Investment (FDI) in developing countries in a globalization framework. The study is done using panel data analysis and cross-section seemingly unrelated regression for 24 developing countries over the period 1976-2005 i.e. for 30 years. The study reveals that the interaction of FDI with some FDI determinants have a strong positive effect on economic progress in developing countries, while the interaction of FDI with the total debt service / GDP and inflation have a negative impact. The study also reveals that the most important determinant of FDI is the communication variable.

Shiralashetti AS and Hugar SS (2009) in their study made an attempt to find out the efforts made by the government of India in bringing FDI inflows in India and overall process in various sections of the Indian
economy in both post-liberalization and pre-liberalization period. The study reveals that the Indian economy has made remarkable progress during the pre-liberalization period. The agricultural sector has progressed through green, yellow, white and blue revolutions. The industrial sector has grown annually by 6%-7%; and the tertiary sector has also contributed a lot to the growth of Indian economy. The study also reveals that there has been continuous efforts made by the government of India in attracting foreign capital during the post-liberalization period which resulted in continuous rise in the inflow of foreign capital on one hand and overall progress in various sectors of the Indian Economy on the other hand.

Krishna Chaitanya Vadiamannati (2009) in his work made an attempt to empirically explore the key determinants of FDI inflows in four South Asian Economies (Pakistan, Sri Lanka, Bangladesh and Nepal) during 1975 to 2006. This study uses five different alternative measures to create ‘India Effect’ and examine its impact on FDI inflows. The study suggested that ‘India Effect’ is positively related to the levels of FDI inflow of its neighbours and the positive impact of FDI inflows on its neighbours is conditioned by Indian economic reforms and negative impact is conditioned by several economic reforms.

Kundan Pokhrel Majagaiya (2009) in his work made an attempt to study the contribution of remittance and FDI, Grants and Pensions; to national Gross Domestic Product (GDP) in Nepal. The data has been analyzed using time series and regression analysis. The study is carried out for a period of 15 years i.e. from 1991 to 2005. The study reveals that
there was no direct way of identifying the linkage between FDI, remittance, grant, pension and GDP. The study further reveals that, in Nepal worker remittance income and grants appear to be the most relevant variables to raise nominal GDP and pension and other items also have significant impact on increasing nominal GDP where as foreign investment seems to be very small in comparison with others.

Sumana Chatterjee (2009) in his thesis made an attempt to investigate and explore the determinants of Foreign Direct Investment in India from the perspective of countries characteristics and also to identify the most significant factors in India that influence foreign investors to invest in India. The issues such as India’s economic integration with world economy, comparative level of FDI among developing countries, major policy initiatives taken to enhance FDI has also been studies with special reference to both inward flows of FDI to India and outward flows of FDI from India. The study has been conducted for the period between 1980-2005. The analysis and results from the study reveals that the motives for both inward and outward FDI are changing. Efficiency seeking investment is gaining more importance as compared to market seeking investment in the case of both domestic and foreign investors. The study also reveals that inward FDI has emerged as an important and contributing factor in influencing outward FDI flows from India.

2.2 STUDIES ON THE IMPACT OF FDI:

Lall and Mohammad (1983) analyzed the impact of foreign ownership on export performance of the largest corporate firms in India using
econometric model. Twenty Four (24) industries containing the largest private-sector companies in India were considered for study. The basic hypothesis was that whether foreign ownership at the industry level had a positive effect on export propensities. The major findings of the study were that foreign presence and the extent of foreign shareholding in firms was positively associated with export propensities. It was also found that the capital intensity has a negative effect on export performance.

Kurwila and Mohan (1996), in their research work made an attempt to explore the impact of industry maturity and stage of development of the host country of Foreign Direct Investment (FDI) on foreign segmental profitability and risk. The objective of this study is to investigate whether firms in growth industries will have a high foreign segmental profitability than declining industry and whether firms operating in emerging regions will have a higher foreign segmental profitability risk than firms operating in developed regions. Accounting based measures of profitability, risk and parametric tests such as ANOVA and ANCOVA were used for data analysis. The study reveals that firms in growth industries had a higher foreign segmental profitability when the variable return on sales was used and lower foreign segmented profitability when return on assets was used. It is also found that the firms operating in emerging regions has a higher profitability than firms operating in developed regions and the firms operating in emerging regions had a significantly higher risk than those operating in developed regions.

Anusuya Yogarajah (1999) in his work made an attempt to look at the impact of liberalisation on FDI in India. This study also covers Pre-1991
and Post-1991 Industrial policies of the government of India, nature and patterns of FDI in India and the factors motivating FDI in India. The study shows that the industrial policies of the Government of India (GOI) are instrumental in attracting FDI inflows and FDI has been in core sectors such as infrastructure, power and coal and the investors are mainly interested in sectors where there is a market for the products. The low costs of labour and non-labour materials and the availability of a market and infrastructure are likely to be the main factors attracting FDI in India.

Chalapati Rao K.S., Murthy MR and Ranganathan KVK (1999), in their work made an attempt to study the Foreign Direct Investment in India in the Post-liberalization period. This study seeks to provide empirical content to the developments during the first seven years of liberalization. The study further revealed that a pattern of FDI inflows in infrastructure is not significant and the increasing dominance of foreign companies in consumer goods sector makes it more significant and FDI approvals in the post-liberalization period are increasing for setting up of subsidiaries.

Luiz R. De Mello (1999) in his paper made an attempt to estimate the impact of Foreign Direct Investment (FDI) on Capital Accumulation and Output and Total Factor Productivity (TFP) growth in recipient economy. The study is conducted for the period of 1970-1990. Time series and panel data analysis are applied for the sample of OECD and non-OECD countries. The study reveals that although FDI is expected to boost long-run growth in the recipients’ economy via technological upgrading and
knowledge spillovers, it is found that the extent to which FDI is growth enhancing depends on substitutions between FDI and domestic investment.

Xiaming Liu David Parker, Kirit Vaiyada and Yinggi Wei (2000) in their study made an attempt to examine the impact of FDI on Chinese electronic industry with special reference to labor productivity. The study is conducted using panel data analysis for 41 sub-sectors of the industry for 1996 and 1997 having different levels of FDI. The results from the analysis of the study show that FDI has a positive impact on labor productivity in Chinese electronics industry. The results further reveals that in terms of relative magnitude of the impact on labor productivity, the human capital is the most important determinant followed by size of the firm and foreign presence.

Ewe-Ghec Lim (2001) in his paper made an attempt to summarize recent arguments/findings on two aspects of foreign direct investment (FDI): its correlation with economic growth and its determinants. The first part of this paper focuses on recent literature regarding positive spillover from FDI while the second deals with the determinants of FDI. The study reveals that while substantial support exists for positive spillover from FDI, there is no consensus on causality. The study also reveals that market size, infrastructure, quality, political/economic stability, and free trade zones are important for FDI, while results are mixed regarding the importance of final incentives, the business/investment climate, labor costs and openness.
Nazir Saeed (2001) in his work made an attempt to study the determinants of FDI in Pakistan and its impact on the economic growth and international trade in Pakistan. The analysis of the study is conducted during the period 1970 to 1999-2000. The result from the study reveals that the share of FDI inflows increased from 21% in 1991 to 50% in 1998. The study reveals that the changes in output level and economic growth are independent of the level of FDI inflows. As far as exports are concerned the study reveals a positive linkage between exports and FDI; and reveals a negative linkage between imports and FDI.

De Backer, Koenraad Frans Maria (2002), in their work made an attempt to analyse how domestic firms and foreign firms differ in industry dynamics and also the impact of foreign direct investment on the economic structure of host countries. The study depicts that the growth path of foreign subsidiaries is totally different from that of domestic firms, with especially young and small firms growing fast within the group of domestic firms. The study also reveals that foreign direct investment is found to discourage domestic entrepreneurship and labour markets.

Ramo Murillo, David (2002), studied the impact of foreign direct investment in the Mexican Industry towards establishment of mechanisms for the transmission of technological spillover with a focus on identification of channels for the transmission of spillovers from FDI to the domestic economy and industry characteristics that influence the possibilities capturing spillover benefits. The methodological approach
followed for conducting this study involves two stages. Firstly, four effects are identified for the transmission of spillovers i.e. linkage, collaboration, demonstration and training effects. Secondly, three industries were selected for analysis i.e. chemicals, pharmaceuticals and electronics. The study finds that foreign presence is associated with a higher rate of introduction of innovations in the production process whereas labor training and industry concentration is negatively associated with the development of mechanisms for the transmission of spillovers. The study also reveals that the current economic and institutional structures have placed constraints on policy choices available to the governments seeking to invest the benefits received from FDI.

Alhakimi, Saif Sallam (2002), in their work made on attempt to examine whether foreign direct investment is associated with high industry wages and also if such activity is also associated with high price-cost margins. The results from this study reveal that statistically significant higher wages in U.S. industries experience high foreign direct investment activity and this FDI activity is associated with low price-cost margins. The results from the study also reveals that industries with significant foreign direct investment are less likely than other industries to pass on higher labor costs to consumers.

Wasantha Athukorala P.P.A. (2003) in his work focuses on the FDI-led growth hypothesis in the case of Sri Lanka with special emphasis on short run and long run relationship between FDI and economic growth and the perception of the civil society, and foreign firms toward FDI. The methodology of this study involves estimating an econometric model as
well as simple calculations such as average and percentages. In this paper the relationship between FDI and GDP has been examined using time series data from the Srilankan economy. The econometric results from this study reveal that FDI inflows don’t exert an independent influence on economic growth and also the direction of causation is from FDI to GDP growth but not GDP growth to FDI. The study also reveals that the investment climate in Srilanka has not improved as a result of political instability and disturbance, direct and indirect regulatory barriers, implied policy instability, poorly developed infrastructure facilities, non liberal trade policy etc.

Pradhan (2004) examined the nature of relationship between the presence of foreign firms and local productivity growth in India pharmaceutical industry and investigated the spillover benefits from Foreign Direct Investment. The export intensity of a firm was hypothesized to have a positive impact on its productivity growth. The results showed that exporting had a negative effect on the efficiency of the firms and reached a modest level of statistical significance.

Zeshan Atique, Mohsin Hasnain Ahmad and Uman Azhar (2004) in their study made an attempt to investigate whether the trade policy regime followed by Pakistan has influenced significantly both the amount of inward FDI received and economic growth. In this paper the effect of trade policy regime on FDI’s contribution to economic growth has been analyzed using time series. The data used in this study is from a period of 1970-2001. The study finds that the growth impact of FDI tends to be greater under an export promotion (EP) trade regime compared to an
import-substitution (IS) regime. The findings of the study suggest that Pakistan’s capacity to progress on economic development will depend on its performance in attracting FDI and the outward looking development strategy of Pakistan should include FDI as an essential part in addition to export promotion strategy.

Zheng, Siler and Giorgioni (2004) examined the impact of Foreign Direct Investment on the export performance of Chinese indigenous firms. This study investigated the impact of FDI inflows into China on export performance using province-level panel data. The study first compared the impact of FDI on exports over the three macro-regions of China—the Coastal, Central and Western regions. The impact of FDI on the exports of indigenous firms within the same three macro-regions has been assessed. Panel data, pooled cross-section and time-series data are employed to study the impact of FDI. The time period considered was 15 years from 1985 to 1999 for estimating the model. Their finding had to be viewed with caution because they did show that FDI had less influence on the export performance of indigenous firms than on all firms (foreign and indigenous). The findings also supported the view that only weak linkages exist between foreign and domestic firms in China. To some extent this may be due to the nature of production undertaking by foreign firms in China.

Jurgen Bitzer and Holger Gorg (2005) in their study made an attempt to investigate the productivity effects of inward and outward Foreign Direct Investment using industry and country level data for 17 OECD countries. The results arrived at from the study reveals that there are a
number of countries which don’t appear to benefit in terms of productivity from inward FDI and on the other hand, a country’s outward FDI is negatively related to productivity. The results also show that there is a substantial heterogeneity in the effect across countries, with a number of countries namely France, Poland, Sweden, UK and US shows positive association between total outward FDI and domestic productivity.

Kulvinder Singh (2005) in his work made an attempt to study the uneven beginning of FDI in India and examined the economic and political developments related to the trends in two sectors: Industry and Infrastructure and sub-sector telecom. The study is a non-empirical and critically covers the uneven beginning, sector-wise unevenness in implementation of policy, yearns and trends that took place from 1991 to 2005. The findings of the study reveal that the government though serious in its efforts to help in growth of economy, started with foreign investment in a haphazard manner. The sectoral analysis reveals that while FDI shows a global increase and has become a staple for success for India, the progress is still hollow. The study further reveals that the impact of the reforms in India on the policy environment for FDI presents a mixed picture.

Raji Kumar Sahoo (2005) in his work made an attempt to review the policy and institutional arrangement for attracting FDI and its patterns of inflows since 1991 and also to empirically estimate the impact of FDI on productivity gap in the manufacturing sector/sub-sectors of India. In this study the impact of FDI on manufacturing sectors growth is estimated by
a limited sample of manufacturing firms comprising of foreign and domestic during the 1991-1998. The study reveals that the role of FDI impacting the productivity growth and its spillovers of productivity to domestic firms is limited in India. Direct impact of FDI in manufacturing sector as a whole and limited to three out of six manufacturing sectors i.e. chemical, electrical and electronics and the indirect impact of FDI (spillovers) in raising productivity of domestic firms is limited to one sector, namely, drugs and pharmaceuticals.

Maathai K Mathiyazhagan (2005) in his study made an attempt to examine the long-run relationship of FDI with gross output, export and labor productivity in Indian economy at the sectoral level. In this study, the panel co-integration (PCONT) test has been used and the annual data from 1990-91 to 2000-01 has been considered for the purpose of data analysis. The results from the study reveals that there is no significance co integrating relationship among variables like FDI, gross output, export and labor productivity in core sectors of the economy. The study also reveals that at the sectoral level of the Indian economy, FDI has helped to raise the output, productivity and export in some sectors only. The results of Panel Co-integration test reveals that a very minimal relationship in variables such as output, labor productivity and export is established by low flow of FDI into India both at the macro level as well as at the sectoral level.

Mona Kansal (2006) in her research work made an attempt to assess the impact of FDI on the growth & development of telecommunication sector and examined the government policies for FDI and development of
telecommunication sector. In this study the impact of foreign direct investments on the development of Indian telecom sector has been analyzed using independently three different types of statistical measures used to find out “cause and effect relationship” between two variables i.e. correlation analysis, time-series analysis and index number analysis. The study reveals that FDI led development of Indian telecommunication sector in the post-liberation period is mainly attributed to the inflows of FDI.

Hugo Rojas – Romangosa (2006) in their study surveyed the recent theoretical and empirical literature in relation to productivity changes that are induced by increased FDI inflows in reference to both the aggregate productivity effects, as well as the spillover effects of FDI on local firms. The study reveals that MNEs are more productive than domestic firms and the FDI inflows directly increase aggregate productivity through a composition effect in the economy. The presence of MNEs also creates indirect effect or spillovers, which can effect local firms in many ways. The study also reveals that positive vertical spillovers outweigh the horizontal spillovers, which are generally close to zero or negative.

Mete Feridum and Yaya Sissoko (2006) in their study made an attempt to examine the relationship between economic growth as measured by GDP per capita and Foreign Direct Investment for Singapore. The study uses data that consists of annual observations during the period between 1977 and 2002. This study employed Granger causality and Vector Auto Regression (VAR) for the purpose of data
analysis. The study reveals that the economic growth as measured by GDP in Singapore is Granger caused by the FDI and the Singapore’s capacity to progress on economic development will depend on the country’s performance in attracting foreign capital.

Santanu Sarkar (2006) in his study examines the relationship between Foreign Direct Investment in an industry sector and the productivity in the domestic firms in the same industry sector. In this study the effect of FDI on firms output in 14 different types of Indian industries has been assessed to find out whether FDI in these industries effect the productivity of domestic firms. This study covers 631 firms from 14 types of Industries for the years 2004-2005. The results from the study reveal that foreign investment in a firm significantly and positively increases the firm’s output and the productivity i.e. the firms with no foreign investment is found to be less productive than the firms with more foreign investment. The result also reveals that there is a negative spillover from foreign investment to domestic firms, particularly in industry sector with more foreign investment. Through the foreign presence in an industry sector brings down the domestic firms output in the same sector, the domestic firms could largely become more productive with the increase in foreign presence in a typical industry sector.

Annika Bergman (2006) in her paper made an attempt to analyze the impact of FDI on India’s domestic pharmaceutical industry through spillover effects and the India’s policy environment in which spillover effects can be materialized. The study mainly focus on the intra-industry
spillover effects, channels through which spillover effects will occur from FDI to local industry and public policies regarding FDI. The analysis of the study shows mixed results in terms of existing spillover effects. The study reveals that the firm with foreign ownership exhibit higher productivity growth than domestically owned firms. It is also concluded that the presence of foreign pharmaceutical firms in India has to some extent contributed to the development of the industry over the years. The study shows varied results about spillover effects in the Indian Pharmaceutical Industry and reveals that spillover effects of FDI are difficult to compute and it is therefore recommended to include a qualitative approach of analysis in addition to the statistical analysis to get a deeper understanding of the effects of foreign firm in an Industry.

Chang & Noorbakhsh (2006) examined the effects of FDI on corporate cash holdings. They had considered two variables to examine the effects of both contemporaneous and expected FDI inflows on international corporate cash holdings. The coefficient for contemporaneous FDI inflows still remained negative and statistically perceived by corporate managers as substitutes for cash. The estimated coefficients for FDI inflows were still negative and statistically different from zero indicating the consistent substitutability between corporate cash holdings and FDI inflows. In case of G-7 countries, it was found that corporate cash holdings are substitutable with FDI. Where as, in case of non G-7 countries, corporate cash holdings and FDI are complementary in nature.

Iftekhar Ahmed Robin (2006) in his study made an attempt to study the impact of Foreign Direct Investment (FDI) on the sectoral growth
pattern of Bangladesh economy with reference to agriculture industry and service sector. The study is carried out for a period of 11 years i.e. from 1995-2005. The data analysis is done by estimating the relationship between FDI inflow and annual output. The Pearson Correlation Coefficient and corresponding P-values are used as tools of data analysis. The analysis of the study reveals that a FDI inflow in Industrial sector doesn’t correlate with industrial growth except for service sector. The study reveals that FDI in agricultural sector doesn’t have any close relationship with sectoral growth pattern and concludes that political tension and lack of investment friendly bureaucratic attitude are often listed by potential investors as major impediments to FDI in Bangladesh.

Pramod Kumar (2006) in his work made an attempt to explore the role of FDI in the economic development of developing countries. The variables such as gross fixed capital formation, gross domestic product are compared with FDI inflows. The study shows that the developing economies have surpassed developed nations in authority FDI and FDI in primary sector has declined but has increased in the service sector. The study also reveals that the role of FDI as a source of capital and technology has grown over time, as other sources of capital have become scarce and FDI is necessary for developing economies to grow rapidly to integrate with international trade and compete with developed economies.

Sudershan K (2007) in his thesis made an attempt to examine the impact of FDI inflows on performance of Indian Pharmaceutical Industry. Econometric modeling such as pooled cross section, time series analysis and panel data analysis are used in the study. The study reveals that
higher proportion of FDI will result into better performance of companies. The study also reveals that FDI has a negative impact on the export performance of FDI-based companies in India.

Philippe Gugler S. Brunner (2007) in this paper made an attempt to assess the effects of FDI on National competitiveness. The study reveals that MNEs potentially have a beneficial impact on the host country, as they are a source of technology in a broad sense and can lead to an upgrading of human capital. The effective impact of FDI depends on the type of activity undertaken and the absorptive capacity of the host state.

Aditya K.R. Bajaj and Swastik Nigam (2007) in this work made an attempt to study the impact of globalization in the pharmaceutical industry and FDI spillovers in various forms to the domestic pharmaceutical industry in terms of domestic productivity and competitiveness. The analysis of the study reveals that the FDI have had spillover effects on the Indian pharmaceutical industry. With the new WTO patent regime introduced in 2005, the foreign players have found greater security in operating in India and due to the spillover effects of a competitive environment, the domestic players have substantially increased their productivity and hence compete on stranger footing with the incoming pharma firms.

Elibariki Msuya (2007) in the study made an attempt to examine the impact of Foreign Direct Investment (FDI) on agricultural productivity and poverty reduction in Tanzania and also the factors that hinder FDI flow to agricultural sector. From the analysis of the study it is observed that FDI has a positive impact on productivity especially to small farmers
who are linked in integrated producer scheme. The study recommends the rethinking of the small institutional setup for increasing productivity and FDI flows to the agricultural sector.

Reddy Dondeti V and Mohanty Bindu B (2007) in their work made an attempt to examine the interrelation among the variables FDI, GDP, exports and imports of the four countries namely China, India, Malaysia and Singapore. Panel data analysis has been used as a primary technique for data analysis. The study reveals that FDI promotes economic growth. The study also provides an estimate that $1 of FDI adds about $3.27 to the GDP of each of these four countries. The analysis also reveals that FDI has no effect on the balance of payment positions of these countries, since its contribution to the growth of exports and imports is nearly the same. The Auto regression model to forecast FDI inflows reveals that China attracts $1.5 bn more FDI than India. It is suggested for the GOI to study some of the policies and strategies adopted by China in order to increase FDI inflows in future.

Muhammad Arshad Khan (2007) in his study made an attempt to examine the link between FDI, domestic financial sectors and economic growth for Pakistan during 1972-2005. In this study the recent econometric technique of co-integration namely the bound testing approach to co-integration has been applied for analysis of the data. The findings of the study reveal that FDI plays an important role in contributing to economic growth and the FDI inflows exerted positive impact on the economic growth in the short-run and long-run. The study also reveals that better domestic conditions not only attract foreign
companies to invest in Pakistan but also allow the host economy to maximize the benefits of foreign investment.

Philippe Gugler and Serge Brunner (2007) in their work made an attempt to provide a comprehensive conceptual framework for assessing the effect of FDI on competitiveness. The study reveals that the effective impact of FDI, however, depends on the type of activity undertaken and the absorptive capacity of the host state. This paper also finds that Ceteris Paribus, clustering is likely to increase the beneficial effects of FDI as the absorptive capacity of firms in a cluster is greater than that of dispersed firms and the aspects such as the activities performed by MNE, the state of economic development, the type of cluster, negative economies of agglomeration etc. determine the concrete impact of FDI on the host economy.

Abdullahi Ahmed, Enjiang Cheng and George Messinis (2007) in their study made an attempt to investigate the short-run and long-run causality relationship between export and FDI, FDI and growth and between export and growth in Sub-Saharan Africa. The data analysis is carried out using Auto Regressive Distributed Lag (ARDL) approach and Granger type test of causality. The study reveals that the FDI trends observed indicates that the share of global FDI inflows has not significantly improved, though the position of Africa’s share improved in recent years. The result shows that bi-directional Granger causality exist between FDI and export in Ghana, Kenya and Nigeria and Granger causality exists from FDI to exports in South Africa and from Exports to FDI in Zambia.
Sambrita Chattopadhyay (2008) in her study made an attempt to examine whether greater inflows of FDI has resulted into an improvement in productivity level of Indian Industrial sector and spillover effects of Foreign Controlled Enterprises (FCFs) in Indian Industry. This study analyzes the impact of the FDI in terms of its spillovers effects and promotion of exports based on both industry and company level data. This study has been conducted for electrical & electronics, Auto-ancillary, Engineering, Chemicals and Pharmaceuticals sector. The study reveals that although India experienced greater magnitude of FDI inflows during economic liberation, the liberal FDI policy of government of India has failed to bring in he “attendant advantages of technology transfer” and “new possibilities for promotion of export”.

Hristijan Todoroski (2008) in his work made an attempt to examine the effects of FDI on employment in the case of Poland. In this study an attempt has been made to explore how foreign capital inflows effect job creation and recent unemployment rate in different economic sectors in Poland from 1991-2007. The theoretical and empirical examinations show influence of FDI on employment creation in polish economy during transaction and after EU membership. The analysis also reveal that FDI harvest had a better influence on employment in other neighboring countries than in Poland as the Polish Economy was not readily responding to utilize FDI.

Satyanarayana Reddy Ch. and Renuka C (2008) in their work made an attempt to analyze the relationship between foreign investment inflows into India and their impact on the macro economic factors like Indian
exports and the net national output / national income. The study reveals that since FDIs are governed by long term considerations and cannot be liquidated, the factors such as long-term political stability, government policies, industrial and economic prospects etc. influence the FDI decision.

Bharathi Kamath G (2008) in this study made an attempt to analyze the impact of Foreign Direct Investment (FDI) on Gross Domestic Product (GDP) and exports in India during the post liberalization period i.e. 1991 to 2005. In this study, simple linear regression analysis was run to analyze the impact of FDI. This study establishes the relationship between the FDI inflows, Exports and GDP in the Indian economy. The analysis of the study reveals that a greater inflow of foreign capital has lead to growth in the exports of goods and services and also growth of the economy over the period of study.

Mojtahed, Ahmad and Hassanzadeh, Ali (2008), in their work made an attempt to study the effect of FDI on productivity and employment. In this paper, panel data across Iran 2– ISIC digit manufacturing industries from 1996 to 2002 has been used to test the spillover effects of FDI inflows on employment in these industries. The results form the analysis of the study reveal that the most important impact of FDI upon the host manufacturing industry is the “spillover effect”. The results show that FDI “spillover effect” exists in many Iranian manufacturing Industries. In oil industries, the spillover effect is positively high and in industries such as textile, paper, plastic, non-material minerals, medical and furniture production, the spillover effect is negative.
Joshua Abor, Charles K.D. Adjasi and Mac-Clara Hayford (2008) in their work made an attempt to examine the export-decision and export-performance of the firms within Ghanian manufacturing sector. The study is carried out from 1991 to 2002 using a profit model. The results from the analysis reveal that there is a positive relationship between FDI and export performance and FDI is very relevant in influencing the export decisions and export performance of Ghanian firms.

Yufen Chen and Jen Chen (2009), in their study made an attempt to analyze the impact of FDI on regional technological capabilities. In this paper firstly the spillover effects of FDI with the reference to actual condition in foreign-funded enterprises in China is analyzed and a comparison is made between foreign funded enterprises and FDI origin countries with reference to R&D expenditures. The analysis is carried out using correlation and regression analysis. The study reveals that impact of FDI on regional technological capability is found to be weak. The study also reveals that the regions with higher technological capabilities will attract higher quantum of FDI inflows; and strong technological availability and huge human capital in domestic firms are essential factors to stimulate the spillover effects of FDI.

Jürger Bitzer and Holger Gorg (Feb. 2009), in their study made an attempt to investigate the productivity effects of inward and outward FDI using industry and country-level data for 17 OECD countries over the period from 1973 to 2001. In this paper, an attempt has been made to explore whether the effects of FDI work through direct compositional effects or changing competition in the host country. The results drawn
from the study reveals that there are on an average productivity benefits from FDI. The study also reveals that stocks of FDI outflows of a country on an average is negatively related to the productivity and a substantial heterogeneity is observed in its effect across OECD countries.

2.3 SUMMARY OF LITERATURE REVIEW:

A brief summary of review of literature is presented below

- It is not that FDI always helps in the economic development; there is another side of this aspect. Since 1960, the discussion on the advantages and disadvantages of FDI has started and is still enduring.
- Even though FDI is allowed in multiple sectors in India, the effects have been good without harming domestic economy.
- The increasing trend of FDI inflows and liberal FDI policy of GOI during the post-liberalization period has failed to bring in the “attendant advantages of technology transfer” and “new possibilities for promotion of exports”.
- Spillover effects of FDI are difficult to compute and it is therefore recommended to include a qualitative analysis in addition to the statistical analysis to get a deeper understanding of the effects of foreign firms in an industry.
- The approval of FDI inflows in the post-liberalization period are increasing for setting up subsidiaries.
- The effective impact of FDI depends on the type of activity undertaken and the absorptive capacity of host state.
• Due to the new WTO patent regime introduced in 2005, the foreign players have substantially increased their productivity, profitability and hence compete on stranger footing with the incoming Pharma Firms.

• Foreign Direct Investment is found to discourage domestic entrepreneurship and labor markets.

• Better domestic foreign conditions not only attract FDI but also allow the host economy to maximize the benefits of FDI.

• The FDI is expected to boost long-run growth in recipient economy via technological upgrading and knowledge spillovers. It is also found that the extent to which FDI is growth enhancing depends upon the degree of complementarity’s and substitutions between FDI and domestic investment.

• The impact of FDI on manufacturing sector reveals that FDI inflows in chemicals, electrical and electronics have direct impact and FDI inflow in drugs and pharmaceutical sectors have indirect impact (spillover effects).

• Greater inflows of foreign capital leads to growth in the exports of goods and services and also growth of economy.

• The low costs of labor and non-labor materials and availability of a market and infrastructure are the main factors attracting FDI inflows in India.

• The impact of FDI varies depending upon host country characteristics and policy environment.
• The growth enhancing effect from FDI seems to vary from country to country and for some countries FDI can even adversely affect the growth process.

• The impact of FDI on India’s pharmaceutical industry in terms of spillover reveals that firms with higher proportion of foreign ownership exhibits higher productivity growth than domestic firms.

• FDI inflows in a firm significantly and positively increases the firm’s output and productivity and higher FDI based firms are more productive than lower FDI based firms.

• Effects of FDI on productivity and employment shows mixed results and though spill over effects exist, it varies from industry to industry.

• FDI inflows in Industrial Sector do not correlate with industrial growth except for service sector.

• Higher proportions of FDI inflows result in better performance of the companies as far as exports are concerned.

• Effective impact of FDI depends upon the type of activity undertaken and absorptive capacity of the Host State.

2.4 RESEARCH GAP:

From the above review of literature, it is found that the topic of ‘Foreign Direct Investment’ has been widely studied at macro and micro level across all the industries and countries. There are mixed results and conclusions. The methodology and models used in most of the studies are subject to limitations in terms of data availability and application of best possible econometric models.
In Indian context, due to the change in Foreign Direct Investment policy across the industries and difficulty in obtaining the firm level data for a longer time period, it is recommended that there is need to study the impact of FDI on performance of the firms (Chibber and Majumdar, 1999). Many of the studies have recommended that future firm-level studies should analyze the possible interaction between foreign competition and domestic firm’s performance (Shapiro, 1983; Trevino and Robber, 2002). It is found that there is a great need for studying the impact of foreign direct investment on export performance of a specific industry. (Siddharthan and Nollen, 2004, Kumar and Siddhartha, 1994, Lall and Mohammad, 1983, Zheng, Siler and Giorgioni, 2004).

It is found in most of the studies that the impact of FDI has been assessed on the macro-economic factors such as GDP, growth rate, forex earnings, employment rate, inflation rate, poverty etc. as well as micro economic factors such as labor productivity, firm level imports, exports, spill over effect (operational efficiency, managerial efficiency) etc., but firm level studies to assess the impact of FDI on the financial performance of FDI-based companies individually and also the impact of magnitude of FDI on the financial performance of FDI-based companies has not been conducted. Further research can also be carried out to examine the impact of FDI on the firm’s performance with special on a particular industry (Sudershanshan K, 2007)

To fill the gap in literature, the present study is carried out focussing on FDI in pharma sector and the impact of FDI on the growth of Indian Pharmaceutical sector in the post-liberalization scenario.
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