Abstract

FDI is one of the most interesting topics in the area of international business and trade. FDI assumes a lot of importance because it can influence many macro economic variables of a host country. It has its impact on employment, prices, exports, imports, exports, balance of payments, economic growth, competition, production etc. FDI represent one of the most important instruments through which a national economy can encourage production, know-how, imports, increase in employment, infrastructure development, poverty reduction, etc. The benefits achieved through the increase in FDIs have created strong competition in the global market of free capital, all with the aim to attract as many and as diverse FDIs as possible. The general trend in the global FDI market is the erasure of geographic borders between developing countries and developed ones as in the past years, developing countries have not only represented a growing FDI market, but have also been aimed at attracting capital intensive investments, as well as R & D investments.

FDI is now widely perceived as an important resource for expediting the industrial development of developing countries especially India because of the fact that it flows as a bundle of capital, technology, skills and some times even market access. Therefore, most of the developing countries offer a welcoming attitude to MNEs that are usually associated with FDI. India's case is a typical in this context because after following a somewhat restrictive policy towards international investment, India liberalized her FDI policy regime
considerably since 1991. And this liberalization has been accompanied by changes in the sectoral composition, entry modes and sources of FDI.

Although conflicting views have been expressed by proponents and opponents of FDI with regard to attracting FDI. But, as a matter of fact, FDI is contemplated the boom of the globalization. In the present era of LPG, no individual country can conceive the idea of all-around development without the judicious mix of foreign capital particularly FDI.

In the present study on 'Growth pattern of FDI in India since liberalization: A case study of Indian insurance sector'; an endeavour is made to examine the major aspects dealing with the inflows of FDI and their impact on the efficiency and effectiveness on the insurance sector. Furthermore, this study examined the issue of increasing the FDI equity limit to 49 per cent and its implications on this sector.

The data used for this study is extensively based on the secondary sources only. Mostly, numerical data for analysis and interpretation has been extracted from various WIRs, Swiss Re Sigma Reports, IRDA Annual Reports, Economic Surveys, SIA Newsletters, RBI Bulletin and RBI’s various Annual Reports. Besides above sources, up to date data was manually collected from FDI data cell, DIPP, Ministry of Commerce and Industry, New Delhi.

The whole thesis is organized in five systematic and continuous chapters. The Chapter - 1 is fully devoted to the introductory and theoretical framework of the study which includes research methodology, review of literature and procedural presentation of conducting the study. More importantly, the researcher has focused on the following objectives of the study: Firstly, to make study with regard
to the introductory background including the significance and utility of FDI in the developing economies like India. Secondly, to examine and assess the various aspects pertaining to the performance of FDI in India in the pre and post-economic liberalization era. Thirdly, to look whether there exists any relationship between FDI, economic reforms and economic growth in India. Fourthly, to appraise inflow of FDI in the Insurance sector in its post reform period. Fifthly, to identify the problems and grey areas in the inflow of FDI in different important sectors of the economy in general and the Insurance sector in particular. Sixthly, to highlight the future prospects of FDI inflow in the Insurance sector and critically examine the implications of increasing FDI from 26 percent to 49 per cent in this sector. And finally to come out with summary and findings of the study to offer some pragmatic suggestions for efficient allocation and attraction of FDI inflows for the larger benefit of Indian economy in general and insurance sector in particular.

Chapter - 2 discusses the different concepts and fundamentals related to FDI process in India. Firstly, this chapter gives a brief outlook of different connotations of FDI as a concept besides various definitions. The researcher made all possible efforts to present an explicit explanation of the concepts and theoretical background of the variables supported by recent and past relevant research studies bearing direct or indirect relation with the topic of present research work.

Chapter - 3 first discusses the different policy phases of FDI vis-à-vis economic liberalization in India and then different patterns of FDI in India is presented. The researcher has divided these policy phases into four to make a systematic and presentable study i.e. Cautious Welcome Policy (1948-67), Selective and Restrictive Phase (1967-79), Partial-Liberalization Phase (1980-90) and Liberalization and Open Door Policy
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(1991 onwards). After this, different patterns, trends and compositions of FDI is highlighted taking state-wise, sector-wise, year-wise, global and source-wise view of the FDI both in the pre and post liberalization period. It starts with different dimensions of FDI flows to India, which includes size and growth, sources and sectoral distribution of FDI inflows. And lastly, after reviewing some related studies, the empirical results that relate to the impact of economic reforms and economic growth on FDI attractiveness and FDI inflows are also presented in this chapter. Before summarizing its results a brief future outlook of FDI is also given in the form of current FDI policy.

Chapter - 4 firstly examines in detail the performance appraisal of Indian insurance sector vis-à-vis entry of private insurers, insurance density, insurance penetration, insurance premium, product development, investment by insurers, corporate agents etc. Present regulatory structure and insurance sector reforms have also been discussed in detail. After this, this chapter examines in detail the different determinants and implications of FDI in insurance sector. In this chapter, the researcher has also presented a theoretical model for increasing FDI cap to 49% in insurance sector.

In the last chapter i.e chapter - 5, the researcher has made every effort to present the conclusion of the present study in a lucid manner. The researcher after making a detailed study of trends, patterns, composition of FDI in the Indian economy in general (in chapter - 3) and FDI in insurance sector in particular (in chapter - 4), has proposed various recommendations and suggestions at the end of this chapter.

Undoubtedly, our economy has benefited enormously from the economic reforms process initiates in July, 1991. The AAGR of GDP has been steadily rising and the 8 per cent plus (annually) growth rate that
is the present norm speaks volumes of how India has been progressing. Besides, inflation has been moderate throughout (except in some recent months due to skyrocketing international prices). The foreign exchange reserves present a very healthy picture and foreign debt is being paid ahead of schedule. India has become a production base and an export hub for diverse goods from agricultural products to automobile components to high end services. Indian firms are now a part of global production chains. Large international corporations have established R & D centres in India. Trade has registered a steady rise and all these factors resulted into greater integration of Indian economy with the world economy. The capital market also has been buoyant and thus India is considered as a favorite destination by foreign investors for their long-term investments like FDI.

The composition of capital inflow has changed significantly over the years. Dependence on aid has vanished and FDI, FPI, ECB and NRI deposits dominate the capital flows. This has been broadly in line with international developments. Unfortunately, the surge in inflows has not been matched by a corresponding growth in the absorptive capacity of the Indian economy. The role of FDI in the up-gradation of technology, skills and managerial capabilities is now well accepted. Additional investments, over and above the investments possible with the available domestic resources help in providing much needed employment opportunities.

The Indian government in the post-liberalization period has slowly but steadily tried to facilitate the inflow of FDI into different sectors of the economy. FDI is sought because it is expected not only to augment investible resources but, more importantly, to improve technological standards, efficiency and competitiveness of domestic
industry. FDI is also associated with bringing in of "relatively" latest technology into the industry since markets for technology are imperfect. However; studies on the impact of FDI on productivity growth suggest that the exact nature of the impact of FDI depends on the firm-industry-host economy specific factors. These include the technological levels prevailing in the industry, the learning capabilities of the firms and the absorptive capacity of the host economy, which determines the rate of technical diffusion of the technology.

FDI in India assumed critical importance in the context of the economic reforms process initiated in 1991. Raising the inflows of FDI substantially was taken as one of the key objectives of industrial and trade reforms. The reforms were accompanied by a rapid increase in inflow of FDI into the Indian economy. India has made significant inroads in opening its economy since it joined the WTO in 1995. There are, however, still remnants of its inward-looking development strategy. Indeed, India’s trade volume as a share of GDP is low in contrast to other major Asian countries and its import tariffs remain comparably high. Moreover; capital account restrictions, in particular, those applying to FDI, are still there, although recent policy directives are laying the ground for greater FDI.\(^1\) However; the prospects for greater world integration are promising, since there is a political consensus on the need to further liberalize trade and capital account restrictions. Moreover, the size and potential for growth of the domestic market is one of the more important factors responsible for the strong interest of foreign investors in India.

\(^1\) The Union Cabinet Reviewed and Approved the FDI Policy recently on 30th June, 2008 for greater FDI inflows and further Liberalization.
From this study, it is observed that in the new era of liberalization when the emphasis is on attracting a large amount of foreign investment, approvals for FDI marked a significant rise as compared to the immediately preceding phase. The approval data reveals that while infrastructure sectors attracted maximum investment, consumer goods sectors also had an important place in the approvals. The broad category of services accounted for almost one-third of the total approvals. The main factors behind the large approved amount appear to be the dereservation of public sector reserved areas, de-licensing, allowing larger share of foreign investors and the general boom in global investment flows.

Size and sector-wise distribution of the approvals suggest that relatively small number of proposals falling under power, fuel and telecommunications sectors account for almost half of the approved investment. However, in view of the large investments and importance of the infrastructure sector, pricing would remain a crucial factor.

It is also observed that since economic liberalization of the Indian economy, the foreign investment particularly FDI has tremendously increased (though it is relatively low when compared with approved investment). The pattern of FDI in terms of country-wise, state-wise and sector-wise has undergone a significant change since economic liberalization in India and has shown an increasing trend which has benefited the whole economy in its growth and development.

From the analysis of all six models through Probit Model and three stage Least-Square Method, it was concluded that during the period under study, economic reforms make a significant positive impact on FDI attractiveness. Thus, it helps international investors to enter into India to cash upon wider opportunities in India. Furthermore,
the interactive effect of reforms and growth is found to have a positive impact on FDI attractiveness. That means economic reforms have positive spillover effects on FDI attractiveness through economic growth. While no significant relationship was found between economic growth and FDI inflows. But it is interesting to note that empirical results proved that economic reforms process helps in increasing FDI inflows and GDP growth rate in India.

It is noteworthy to point out that in India a number of studies have been undertaken on FDI, but till now, hardly any study has taken into account the trend and pattern and more importantly the impact of FDI in Insurance sector.\(^2\) This study is thus, an attempt to analyze in detail the implications of FDI in the Indian insurance sector besides suggesting some prudent measures to make this sector vibrant and efficient so as to contribute significantly for the growth and development of our economy.

It is a fact that insurance industry in the Indian economy is very pertinent for its smooth and balanced development. The industry contributes to GDP and acts as a catalyst to accelerate the growth of the economy. Besides contributing to the GDP, insurance industry also has a great social significance. It is associated with disasters, calamity and loss and suffering, which cause turbulence in industry, commerce and community. Insurance companies generate funds out of insurance premium collected and help in uplifting the economy. The companies also provide jobs for hundreds of thousands and dispense dividend income to their shareholders. Major contribution of the sector lies in the kind of employment opportunity it has created in the last few years.

\(^2\) None is available till now for the Indian economy.
with 20000 jobs through direct employment and 300000 through indirect employment and outsourcing.

It is pertinent to point out that currently India’s economy is growing 7-8 per cent annually, one of the fastest in the world. But many experts fear lack of adequate infrastructure could slow progress in the coming years. The country needs huge investment in building power plants, roads and ports to keep pace with the demand of rapidly growing economy. Therefore, a well-developed and evolved insurance sector is needed for economic development as it provides long-term funds for infrastructure development and at the same time strengthens the risk taking ability. It is estimated that over the next 10 years, India would require investment of the order of US$ 1 trillion. The insurance sector, to some extent, can enable investment in infrastructure development to economic growth of the economy.

With a large capital outlay and long gestation periods, infrastructure projects are fraught with a multitude of risks throughout the development, construction and operation stages. These include risks associated with project implementation, including geological risks, maintenance, commercial and political risks. Without covering these risks, the financial institutions are not willing to commit funds to the sector, especially because the financing of most private projects is on a limited or non-recourse basis. Thus, insurance companies not only provide risk cover to infrastructure projects, they also contribute long-term debt and equity for infrastructure projects. Infact, insurance companies are an ideal source of long-term debt and equity for infrastructure projects. With long-term liability, they get a good asset-liability match by investing their funds in such projects. Thus, insurance companies prove fruitful for the long term development of an economy.
The Indian insurance market has undergone a significant change over the last nearly 8 years largely due to the regulatory and structural changes. Premium growth is now being driven by other factors such as the growing consumer class, increased FDI, infrastructure development, and an increased awareness of catastrophe exposure. Despite significant positive changes, the insurance market still faces the challenge of poor customer perceptions and the danger that the pace of reform will slow.

It is a well accepted fact that due to the presence of large number of private insurers, Indian insurance industry has, in the last 8 years, grown enormously and performed well. Overall this industry has shown positive signs in-terms of insurance penetration, density, number of players, premiums, number of policies and products, investments, fulfillment of social and rural obligations, corporate agents, brokers and providing insurance cover to the poor and needy.

Recently in 2007, Planning Commission constituted a Committee on service sector, Chaired by Planning Commission member, Anwarul Hooda, and this committee suggested that ‘the insurance sector in India is in a high-growth phase with substantial investment requirements, permitting foreign investors to own a larger share may be considered’. The effect of this change will make two big changes. Firstly, it will increase the focus of the existing private insurers operating within the Indian market. As this has been discussed in the study at length that the private insurers are increasingly diverging on strategy as they are influenced by their foreign ownership will lead to differentiated strategy like more niche players and a wider product range. Secondly, it is expected to increase the supply and the capacity in the market as new investors will decide to enter the market. Indeed, a number of insurers have committed that as soon as foreign companies are allowed more