CHAPTER I

INTRODUCTION

Investment is a key factor in economic growth. In empirical studies the world around, there is no doubt regarding the positive relationship between high investment rates and high growth rates. According to UNCTAD (1999), countries that devote high proportion of output to investment may sustain more rapid growth than countries that invest less. Investment is mainly financed by domestic savings. But developing countries short of domestic savings find it difficult to contribute towards high investment rates. FDI brings a relief to such countries by bringing non-debt creating inflows of foreign capital. The emphasis on the role of FDI as a package of investment and skills to act as an instrument in increasing investment and growth in the host country is increasing by the day.

The flows of foreign investments take the form of direct investment and portfolio investment which are non-debt creating flows in nature. Portfolio investment does not seek management control, but is motivated by profit. Portfolio investment occurs when individual investors invest, mostly through stockbrokers in stocks of foreign companies in foreign land in search of profit opportunities. Foreign investment comes in host country through various route and many forms. Among all various routes, the two main routes are Foreign
Direct investment (FDI) and Foreign Indirect Investment (FII) (Jasbir Singh et. al. 2012).

Inflow of investment from other countries is encouraged since it complements and stimulates domestic investments in capital-scarce economies of developing countries. FDI brings not just capital but also better management and governance practices and often technology transfer (Syed Tabassum Sultana and Pardhasaradhi 2012).

The world has been globalizing and all the countries are liberalizing their policies for welcoming investment from countries which are abundant in capital resources. The countries which are developed are focusing on new markets where there is availability of abundant labours, scope for products, and high profits. Therefore Foreign Direct Investment (FDI) has become a battle ground in the emerging markets. The objective behind allowing FDI is to complement and supplement domestic investment, for achieving a higher level of economic development and providing opportunities for technological upgradation, as well as access to global managerial skills and practices (Syed Azhar and Marimuthu 2012).

In India, the importance of FDI and technology needs no emphasis. India being a developing country with a huge population and low per capita income, the domestic savings are very meagre. This shortfall in domestic savings can be filled by FDI so that, the productive capacity of the economy is augmented to achieve
the goal of sustained investment and growth. The support for FDI stems from the expectation of spillover effect that has been propagated as a major benefit occurring from this form of investment. It is expected to help the domestic sector in obtaining sufficient foreign capital at lower costs as well as help it acquire sophisticated technology through association with foreign firms (Aditya Mohan Jadhav and Nagi Reddy 2013).

In 1991 some radical amendments were made in the economic policy of India through the New Economic Policy (NEP). The policy observed that while freeing the Indian economy from official controls, opportunities for promoting foreign capital and technology in India, should also be fully exploited. In this direction, the NEP liberalised, privatised and globalised the Indian economy towards foreign investments and technology (Prasanna 2010).

FDI inflows to India witnessed significant moderation in 2010-2011 while other emerging market economies in Asia and Latin America received large inflows. This had raised concerns in the wake of widening current account deficit in India beyond the perceived sustainable level of 3.0 per cent of GDP during April-December 2010. This also assumes significance as FDI is generally known to be the most stable component of capital flows needed to finance the current account deficit. Moreover, it adds to investible resources, provides access to advanced technologies, assists in gaining production know-how and promotes exports. India’s approach towards foreign investment has been relatively
conservative to begin with, it progressively started catching up with the more liberalised policy stance of other Emerging Market Economies from the early 1990s. This progressive liberalisation, coupled with considerable improvement in terms of macroeconomic fundamentals, reflected in growing size of FDI flows to the country that increased nearly 5 fold during first decade of the present millennium (Reserve Bank of India 2013).

Though the liberal policy stance and strong economic fundamentals appear to have driven the steep rise in FDI flows in India over past one decade and sustained their momentum even during the period of global economic crisis (2008-09 and 2009-10), the subsequent moderation in investment flows despite faster recovery from the crisis period appears somewhat inexplicable.

The FDI inflows grow at about 20 times since the opening up of the economy to foreign investment. India received maximum amount of FDI form developing economies. It is found that there is a huge gap in FDI approved and FDI realized. It is observed that the realization of approved FDI into actual disbursements has been quite slow. The reason of this slow realization may be the nature and type of investment projects involved. Beside this, increased FDI has stimulated both exports and imports contributing to rising levels of international trade. Further, the explosive growth of FDI gives opportunities to Indian industry for technology up gradation, gaining access to global managerial skills and
practices, optimizing utilization of human and natural resources and competing internationally with higher efficiency. (Girbal Singh Lodhi 2014).

1.1 FDI IN THE GLOBAL LEVEL

Foreign Direct Investment has appeared as the most significant source of external resource flows to developed countries, developing countries and under developed countries (Sarbapriya Ray 2012).

**TABLE 1.1**

<table>
<thead>
<tr>
<th>Year</th>
<th>FDI Inflows</th>
<th>Year</th>
<th>FDI Inflows</th>
<th>Year</th>
<th>FDI Inflows</th>
</tr>
</thead>
<tbody>
<tr>
<td>1991</td>
<td>153981.0</td>
<td>2000</td>
<td>1358820.4</td>
<td>2009</td>
<td>1181412.2</td>
</tr>
<tr>
<td>1992</td>
<td>162925.2</td>
<td>2001</td>
<td>683765.4</td>
<td>2010</td>
<td>1388821.0</td>
</tr>
<tr>
<td>1993</td>
<td>220111.9</td>
<td>2002</td>
<td>589808.9</td>
<td>2011</td>
<td>1566839.0</td>
</tr>
<tr>
<td>1994</td>
<td>254916.1</td>
<td>2003</td>
<td>550588.8</td>
<td>2012</td>
<td>1510918.3</td>
</tr>
<tr>
<td>1995</td>
<td>341523.1</td>
<td>2004</td>
<td>688233.0</td>
<td>2013</td>
<td>1427180.9</td>
</tr>
<tr>
<td>1996</td>
<td>388758.8</td>
<td>2005</td>
<td>950125.0</td>
<td>2014</td>
<td>1276999.3</td>
</tr>
<tr>
<td>1997</td>
<td>481500.6</td>
<td>2006</td>
<td>1402125.9</td>
<td>2015</td>
<td>1762155.0</td>
</tr>
<tr>
<td>1998</td>
<td>692331.0</td>
<td>2007</td>
<td>1902244.5</td>
<td>2016</td>
<td>1746423.5</td>
</tr>
<tr>
<td>1999</td>
<td>1076382.4</td>
<td>2008</td>
<td>1497788.1</td>
<td>2017</td>
<td>1429809.4</td>
</tr>
</tbody>
</table>

Source: World Investment Report
Table 1.1 shows the amount of FDI inflows in the world level during the period from 1991 to 2017. In the year 1991 the amount of inflows in the world level was US $ 153981.0 million. It had tremendously increased over the ten years period from 1991 to 2000 and reached the maximum of US $ 1358820.4 million in the year 2000. In the year 2001 the amount of foreign direct investment at the world level was US $ 683765.4 million and in the following two years there was a declining trend and it declined to US $ 550588.8 million in the year 2003. From 2004 onwards there was a continuous increase and it reached US $ 1566839.0 million in the year 2011. It declined to US $ 1276999.3 million in the year 2014 and later on it began to increase.

1.2 FDI INFLOWS IN THE DEVELOPED ECONOMIES

FDI is critical for emerging market economies. Their companies need the multinationals’ funding and expertise to expand their international sales. The developed countries need private investment in infrastructure, energy and water to increase jobs and wages. They also need FDI for restructuring or refocussing their core businesses.
TABLE 1.2

FDI INFLOWS IN THE DEVELOPED ECONOMIES (1991 to 2017)  
(Amount in US $ million)

<table>
<thead>
<tr>
<th>Year</th>
<th>FDI Inflows</th>
<th>Year</th>
<th>FDI Inflows</th>
<th>Year</th>
<th>FDI Inflows</th>
</tr>
</thead>
<tbody>
<tr>
<td>1991</td>
<td>114524.1</td>
<td>2000</td>
<td>1120505.8</td>
<td>2009</td>
<td>654366.7</td>
</tr>
<tr>
<td>1992</td>
<td>107816.0</td>
<td>2001</td>
<td>459713.6</td>
<td>2010</td>
<td>699889.2</td>
</tr>
<tr>
<td>1993</td>
<td>141395.9</td>
<td>2002</td>
<td>413024.4</td>
<td>2011</td>
<td>817414.8</td>
</tr>
<tr>
<td>1994</td>
<td>150599.0</td>
<td>2003</td>
<td>337172.0</td>
<td>2012</td>
<td>787358.8</td>
</tr>
<tr>
<td>1995</td>
<td>219763.7</td>
<td>2004</td>
<td>395517.7</td>
<td>2013</td>
<td>680275.0</td>
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<tr>
<td>1996</td>
<td>236342.3</td>
<td>2005</td>
<td>587704.8</td>
<td>2014</td>
<td>522042.9</td>
</tr>
<tr>
<td>1997</td>
<td>286293.0</td>
<td>2006</td>
<td>940318.3</td>
<td>2015</td>
<td>962496.3</td>
</tr>
<tr>
<td>1998</td>
<td>508530.2</td>
<td>2007</td>
<td>1289493.5</td>
<td>2016</td>
<td>1133245.2</td>
</tr>
<tr>
<td>1999</td>
<td>852937.6</td>
<td>2008</td>
<td>801909.2</td>
<td>2017</td>
<td>712382.9</td>
</tr>
</tbody>
</table>

Source: World Investment Report

Table 1.2 explains the FDI inflows in the developed economies during 1991 to 2017. The amount of FDI inflows in the developed economies has increased to US $ 712382.9 million in the year 2017 from US $ 114524.1 million in the year 1991. In the first decade after globalisation of Indian economy there was a drastic change in the inflows and it increased continuously. But in the second and third decade after globalisation there were some ups and downs in the FDI inflows.
1.3 FDI INFLOWS IN THE DEVELOPING ECONOMIES

FDI is considered a key element for a country’s economic integration and represents key source to finance capital investment. FDI improves the transfer of technology and know-how, increases competition and pushes for more positive development of firms in the developing economies. So the developing economies seek FDI to improve their economic growth.

**TABLE 1.3**

**FDI INFLOWS IN THE DEVELOPING ECONOMIES (1991 to 2017)**
(Amount in US $ million)

<table>
<thead>
<tr>
<th>Year</th>
<th>FDI Inflows</th>
<th>Year</th>
<th>FDI Inflows</th>
<th>Year</th>
<th>FDI Inflows</th>
</tr>
</thead>
<tbody>
<tr>
<td>1991</td>
<td>39318.3</td>
<td>2000</td>
<td>232390.3</td>
<td>2009</td>
<td>465306.6</td>
</tr>
<tr>
<td>1992</td>
<td>53458.2</td>
<td>2001</td>
<td>215793.8</td>
<td>2010</td>
<td>625330.3</td>
</tr>
<tr>
<td>1993</td>
<td>75691.3</td>
<td>2002</td>
<td>166739.0</td>
<td>2011</td>
<td>670149.3</td>
</tr>
<tr>
<td>1994</td>
<td>102382.5</td>
<td>2003</td>
<td>195584.2</td>
<td>2012</td>
<td>658773.7</td>
</tr>
<tr>
<td>1995</td>
<td>117760.9</td>
<td>2004</td>
<td>263718.3</td>
<td>2013</td>
<td>662405.6</td>
</tr>
<tr>
<td>1996</td>
<td>147078.3</td>
<td>2005</td>
<td>331752.1</td>
<td>2014</td>
<td>698493.6</td>
</tr>
<tr>
<td>1997</td>
<td>185400.8</td>
<td>2006</td>
<td>402982.8</td>
<td>2015</td>
<td>764670.4</td>
</tr>
<tr>
<td>1998</td>
<td>176632.4</td>
<td>2007</td>
<td>525525.0</td>
<td>2016</td>
<td>646030.4</td>
</tr>
<tr>
<td>1999</td>
<td>216.289.5</td>
<td>2008</td>
<td>578482.2</td>
<td>2017</td>
<td>670658.0</td>
</tr>
</tbody>
</table>

Source: World Investment Report
Table 1.3 shows the amount of foreign direct investment inflows into developing countries during 1991 to 2016. The total foreign direct investment to developing countries was US $ 39318.3 million in the year 1991. After that there was a continuous increase in the foreign direct investment inflows up to the year 2000 except 1998. In 1998 there was a down trend and the amount of foreign direct investment was US $ 176632.4 million. During the next ten years there was moderate fluctuations in the inflows. In 2002 the amount of inflows decreased from US $ 215793.8 million in the year 2001 to US $ 166739.0 million. Then it started to increase and attained US $ 578482.2 million in the year 2008. It declined to US $ 465306.6 million in the year 2009 and then increased to US $ 625330.3 million in the year 2010. In the third decade after globalisation the maximum FDI inflows occurred in the year 2015, which was US $ 764670.4 million and it decreased to US $ 670658.0 million in the year 2017.

1.4 FDI IN INDIA

The FDI flows in India took a new turn with announcement of New Economic Policy in 1991. The last decade of the 20th century witnessed a drastic increase in foreign direct investment, accompanied by a marked change in the attitude of most developing countries towards inward investment. The period after 1991 is termed as post liberalization period during which not only the quantum of FDI to India escalated but the sector-wise composition of FDI also underwent incredible change (Mamta sharma, Satbir Singh 2013). The list of investing
countries to India reached to 150 in 2010 as compared to 29 countries in 1991 (Mahanta Devajit 2012). According to “World Investment Report 2011”, from a position of 8th rank in 2009 India has fallen to 14th position as country attracting largest FDI. A number of studies and reports highlight the weakness of India as a falling FDI destination. It is a challenge for a developing country like India to channelize its capital inflow through FDI into a potential source of productivity gain for domestic firms. The initiatives taken by the government of India the FDI inflows have shown a rising trend from 1991 to 2017. The rise in flows of FDI till 1997 was due to not only of the liberalization policy but also due to the sharp expansion in the global scale of FDI outflows during the 1990s. Then after 1998-99 and 1999-00 there was decline in FDI inflow which was due to the decline in industrial growth rate in the economy and also due to the result of the East Asian Financial Crisis. But again in the next following year, foreign investment started to bounce back. During 2002-03 and 2003-04, again there was fall in flow of foreign direct investment which was due to the cast of Global Recession on the Indian economy (Sarbapriya Ray 2012). The measures introduced by the government to liberalise provisions relating to FDI in 1991 increased FDI from US $ 97 million in 1990 to US $ 42215 million in 2017.

The government has made changes to the FDI policy by opening up more sectors. The following table shows the sector wise FDI limits and its entry routes according to the new policy of August 2017.
Table 1.4

Sector Wise FDI Limits

<table>
<thead>
<tr>
<th>Sector</th>
<th>FDI limit</th>
<th>Entry Route</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agriculture and Animal Husbandry</td>
<td>100%</td>
<td>Automatic</td>
</tr>
<tr>
<td>Plantation sector</td>
<td>100%</td>
<td>Automatic</td>
</tr>
<tr>
<td>Mining</td>
<td>100%</td>
<td>Automatic</td>
</tr>
<tr>
<td>Petroleum and Natural Gas</td>
<td>100%</td>
<td>Automatic</td>
</tr>
<tr>
<td>Defence Manufacturing</td>
<td>100%</td>
<td>Automatic up to 49% above 49% under government route</td>
</tr>
<tr>
<td>Broadcasting</td>
<td>100%</td>
<td>Automatic</td>
</tr>
<tr>
<td>Broadcasting Content Services</td>
<td>49%</td>
<td>Government</td>
</tr>
<tr>
<td>Up-linking of Non-‘News &amp; Current Affairs’ TV Channels/ Down-linking of TV channels</td>
<td>100%</td>
<td>Automatic</td>
</tr>
<tr>
<td>Print Media</td>
<td>26%</td>
<td>Government</td>
</tr>
<tr>
<td>Civil Aviation – Airports</td>
<td>100%</td>
<td>Government</td>
</tr>
<tr>
<td>Civil Aviation – Air Transport Services</td>
<td>100%</td>
<td>Automatic up to 49% above 49% under government route</td>
</tr>
<tr>
<td>Category</td>
<td>Percentage</td>
<td>Type</td>
</tr>
<tr>
<td>-------------------------------------------------------------------------</td>
<td>------------</td>
<td>-----------------</td>
</tr>
<tr>
<td>Civil Aviation</td>
<td>100%</td>
<td>Automatic</td>
</tr>
<tr>
<td>Construction Development: Townships, Housing, Built-up Infrastructure</td>
<td>100%</td>
<td>Automatic</td>
</tr>
<tr>
<td>Industrial Parks (new &amp; existing)</td>
<td>100%</td>
<td>Automatic</td>
</tr>
<tr>
<td>Satellites-establishment and operation, subject to the sectoral guidelines of Department of space/ ISRO</td>
<td>100%</td>
<td>Government</td>
</tr>
<tr>
<td>Private Security Agencies</td>
<td>74%</td>
<td>Automatic up to 49% above 49% and up to 74% under government route</td>
</tr>
<tr>
<td>Telecom Services</td>
<td>100%</td>
<td>Automatic up to 49% above 49% under government route</td>
</tr>
<tr>
<td>Cash &amp; Carry Wholesale Trading</td>
<td>100%</td>
<td>Automatic</td>
</tr>
<tr>
<td>E-commerce activities</td>
<td>100%</td>
<td>Automatic</td>
</tr>
<tr>
<td>Single Brand retail trading</td>
<td>100%</td>
<td>Automatic up to 49% above 49% under government route</td>
</tr>
<tr>
<td>Multi Brand Retail trading</td>
<td>51%</td>
<td>Government</td>
</tr>
<tr>
<td>Duty Free shops</td>
<td>100%</td>
<td>Automatic</td>
</tr>
<tr>
<td>Railway Infrastructure</td>
<td>100%</td>
<td>Automatic</td>
</tr>
<tr>
<td>Asset Reconstruction Companies</td>
<td>100%</td>
<td>Automatic</td>
</tr>
<tr>
<td>-----------------------------------------------</td>
<td>------</td>
<td>-----------</td>
</tr>
<tr>
<td>Banking Private Sector</td>
<td>74%</td>
<td>Automatic up to 49% above 49% and up to 74% under government route</td>
</tr>
<tr>
<td>Banking public sector</td>
<td>20%</td>
<td>Government</td>
</tr>
<tr>
<td>Credit Information Companies</td>
<td>100%</td>
<td>Automatic</td>
</tr>
<tr>
<td>Infrastructure Company in the Securities Market</td>
<td>49%</td>
<td>Automatic</td>
</tr>
<tr>
<td>Pension Sector</td>
<td>49%</td>
<td>Automatic</td>
</tr>
<tr>
<td>Insurance</td>
<td>49%</td>
<td>Automatic</td>
</tr>
<tr>
<td>Power Exchanges</td>
<td>49%</td>
<td>Automatic</td>
</tr>
<tr>
<td>White Label ATM Operations</td>
<td>100%</td>
<td>Automatic</td>
</tr>
<tr>
<td>Pharmaceuticals (Green Field)</td>
<td>100%</td>
<td>Automatic</td>
</tr>
<tr>
<td>Pharmaceuticals (Brown Field)</td>
<td>100%</td>
<td>Automatic up to 74% above 74% under government route</td>
</tr>
<tr>
<td>Food products manufactured or produced in India</td>
<td>100%</td>
<td>Government</td>
</tr>
</tbody>
</table>

Source: www.rbi.org.in
FDI is prohibited in the following sectors. Lottery business including Government/private and online lotteries, Gambling and betting including casinos, chit funds, Nidhi company, trading in transferable Development Rights (TDRs), real estate business or construction of Farm Houses, manufacturing of cigars, cheroots, cigarillos and cigarettes, of tobacco or of tobacco substitutes.

1.5 FDI POLICY FRAMEWORK IN INDIA

There has been a drastic change in the policy framework towards foreign direct investment in India.

1.5.1 Pre-Globalisation period

The historical background of FDI in India can be traced back with the establishment of East India Company of Britain. British capital came to India during the colonial era of Britain in India. But after the Second World War, Japanese companies entered Indian market and enhanced their trade with India, yet United Kingdom remained the most dominant investor in India. After independence issues relating to foreign capital and operations of multinational companies gained attention of the policy makers. Because of this the policy makers designed the FDI policy which aims FDI as a medium for acquiring advanced technology and to mobilise foreign exchange resources. Then the industrial policy of 1965, allowed multinational companies to venture through
technical collaboration in India. Therefore, the government adopted a liberal attitude towards FDI policy (Bhavya Malhotra 2014).

After 1948 the government of India evolved a complex legal and institutional control under the Foreign Exchange Restriction Act and Monopolies Restrictive Trade Practice Act to ensure a marginal and highly circumscribed role of FDI in the economy. As a result the nominal ceiling on foreign equity participation was limited to 40 per cent and FDI was largely restricted to priority industries requiring sophisticated technology, under takings with high export-orientation and industries in which a critical production gap existed. By the early 1980s it was felt that these restrictions have discouraged foreign investment which could enhance efficiency by bringing superior technologies and better work practices. This led to some liberalization in the Industrial Policy Statements of 1980 and 1982. By 1983, large industrial groups and foreign companies were no longer restricted from producing transport machinery and tools, electric equipment, chemical and pharmaceutical products and industrial machinery. By the mid-1980s non-resident Indians were allowed to invest in Indian companies through equity participation. The establishment of four additional export-processing zones was announced in 1985 with a view of attracting export-oriented FDI (Kishor Sharma 2000)
1.5.2 Post Globalisation Period

Foreign Investment in India is governed by the FDI policy announced by the Government of India and the provision of the Foreign Exchange Management Act (FEMA) 1999. The Reserve Bank of India (RBI) in this regard had issued a notification, which contains the Foreign Exchange Management (Transfer or issue of Security by a person resident outside India) Regulations, 2000. This notification has been amended from time to time. The Ministry of Commerce and Industry, Government of India is the nodal agency for motoring and reviewing the FDI policy on continued basis and changes in sectoral policy or sectoral equity cap. The FDI policy is notified through Press Notes by the Secretariat for Industrial Assistance (SIA), Department of Industrial Policy and Promotion (DIPP). The foreign investors are free to invest in India, except few sectors or activities, where prior approval from the RBI or Foreign Investment Promotion Board (FIPB) would be required (Kali Ram Gola et. al. 2013).

The Ministry of Home Affairs has finally given the approval to the proposal of allowing FDI in railways. The Cabinet Committee on Economic Affairs (CCEA) is expected to consider the proposal. Foreign investors can invest only in construction and maintenance of railway projects, and not in operations.

The former Prime Minister Dr. Manmohan Singh has sought increased Japanese investment in the country. The presence of Japanese companies in the
field of manufacturing and research and development in the electronic industry and energy saving technologies has increased a lot.

In an effort to improve capital flows into the country, the Indian government has allowed 100 percent FDI under automatic route in storage and warehousing, which includes warehousing of agriculture products with refrigeration. The government has also set up National Centre for Cold Chain Development (NCCD) which will look at standards and protocols for cold chain infrastructure (Bhavya Malhota 2014).

Make in India was launched by the government of India on 25 September 2014 to encourage companies to manufacture their products in India and also increase their investment. After the launch, India received investment commitments worth US $ 24 billion and investment inquiries worth US $ 22 billion between September 2014 and February 2016. This programme is designed to facilitate investment, foster innovation, enhance skill development, protect intellectual property and build best manufacturing in the country.

The primary objective of this initiative is to attract investments from across the globe and strengthen India’s manufacturing sector. The Make in India programme is very important for the economic growth of India as it aims at utilising the existing Indian talent base, creating additional employment opportunities and empowering secondary and tertiary sector. The programme also aims at improving India’s rank on the ease of doing business index by eliminating
the unnecessary laws and regulations, making the government more transparent, responsive and accountable.

1.6 Types of FDI

Following are the types of foreign direct investment.

1.6.1 Green Field Investment

This type of investment is made for providing new facilities or expanding the existing facilities. This investment creates new production capacity and job, transfer technology and know-how and can lead to link with the global markets.

1.6.2 Mergers and Acquisition

This is the primary type of FDI. Transferring of existing assets from local firms to foreign firms takes place under this type of investment.

1.6.3 Cross-Border Acquisition

The control and operations of assets are transferred from a local to a foreign company, with the local company becoming an affiliate of the foreign company.

1.6.4 Horizontal Foreign Direct Investment

Under this type, investment is made in the same industry abroad as a firm operates in at home.
1.6.5 Vertical Foreign Direct Investment

This type of investment is further divided into two types.

a) Backward Vertical FDI: where an industry located in abroad provides inputs for a firm’s domestic production process.

b) Forward Vertical FDI: where an industry in abroad sells the outputs of a firm’s domestic production processes. (Jayakumar et. al. 2014)

1.7 IMPACT OF FDI

Foreign direct investment has appeared as the most significant source of external resource flows to developing countries. It impacts in the host country’s economic growth, augment in the productivity, boost in exports and improves the balance of payments position, amplified pace of transfer of technology and the increase in the employment position.

1.7.1 FDI AND GDP

Economic growth is a narrower concept than economic development. It is an increase in a country’s real level of national output which can be caused by an increase in the quality of resources, increase in the quantity of resources and improvements in technology or in another way an increase in the value of goods and services produced by every sector of the economy. Economic growth can be measured by an increase in a country’s GDP that is a positive change in the level of production of goods and services by a country over a certain period of time.
Nominal growth is defined as economic growth including inflation, while real growth is nominal growth minus inflation. Economic growth is usually brought about by technological innovation and positive external forces. Growth relates to a gradual increase in one of the components of Gross Domestic Product: consumption, government spending, investment, net exports. Quantitative measurement and effects of quantitative changes in the economy increase real GDP. Economic growth is a more relevant metric for progress in developed countries. But it is widely used in all countries because growth is a necessary condition for development and scope is growth concerned with increase in the economy’s output.

Gross domestic product in simple means the sum of final value of goods and services producing within the domestic territory of the country in an accounting period. It reflects the potential market size of the Indian economy. In India, Gross domestic product is calculated at market price and at factor cost (Dr. Mohd. Yameen and Izhar Ahmad 2015). From 1996 until 2013, India’s GDP growth rate averaged 1.6 percent reaching an all-time high of 5.8 percent in December of 2003 and a record low of -1.7 percent in March of 2009. In India, the growth rate in GDP measures the change in the seasonally adjusted value of the goods and services produced by the Indian economy during the quarter. The most important and the fastest growing sectors of Indian economy are services, trade, hotels, transport and communication; financing, insurance, real estate and
business services and community, social and personal services account for more than 60 percent of GDP. Agriculture, forestry and fishing constitute around 12 per cent of the output, but employ more than 50 per cent of the labour force. Manufacturing accounts for 15 per cent of GDP, construction for another 8 per cent and mining, quarrying, electricity, gas and water supply for the remaining 5 per cent. In the fourth quarter of 2013, Indian economic growth slowed to 4.7 per cent over a year earlier, down from a 4.8 per cent expansion in the previous period, hurt by a contraction in manufacturing and mining output (Mahesh Kumar 2014).

1.7.2 FDI and BALANCE OF PAYMENTS

The true picture of international obligations of a country can be studied only with the help of balance of payments position. It will not be possible for every country to have always surplus balance or favourable balance in the international payments (Sankaran 1997). A country’s balance of payments position is greatly influenced by the nature of its international capital flows and also its economic policy (Sethi 1996).

Having a stable balance of payment is a pre-requisite for any economy in the current globalised world. Foreign direct investment helps to strengthen a country’s balance of payment by way of additional foreign exchange earning possibly through exports of goods and services especially from the firms which receive the FDI (Kavitha 2012).
In India, FDI inflows are integral part of capital account of India’s Balance of Payments (BoP). India’s balance of payment has improved considerably from US $ 2,492 million in 1991 to US $ 21550 million in 2016-17. FDI is non-debt financing source and statistics explain that there is a shift from reliance on debt flows to non-debt flows like FDI from 1993 onwards. The major contributing factor for this positive Balance of Payment position is surplus capital account balance which, in turn, is due to huge FDI inflows. But India is facing the problem of current account deficit since 1960s and the trend is still continuing. The amount of deficit rose from US $ -824 million in 1960-1961 to US $ -38,411 million in 2009-10. Statistics reveal that trade deficit plays a major in causing current account deficit. FDI not only affects the domestic investment climate but also influences foreign trade by import and export of goods and services. However, the resultant impact whether it will improve or deteriorate the trade position depends on the magnitude of the two forces, namely, exports and imports (Manpreet Kaur, Vinayshil Gautam 2012).

Though India’s export basket was limited, the sharp devaluation clearly increased the competitiveness of India’s exports. Concurrently, India had to undertake a number of trade liberalising measures. India’s current account particularly remains vulnerable to developments in the trade account. It is evident from the size of trade deficit growing from 0.5 per cent of GDP during 1951-55 to 8.7 per cent during 2007-12. In 2011-12, the current account deficit has widened
to a record 4.2 per cent of GDP. Over the years, current account derived some resilience from surplus generated by invisibles, particularly software exports and private transfers, but trade deficit continues to dictate the overall trend in the current account. Whenever trade account worsens reflecting downswings in the global business cycle or rise in international oil prices, the current account also comes under stress. Since India’s linkage with the world economy, in terms of trade and finance, is likely to grow further, it is important that resilience in its trade account is built up mainly by promoting productivity based export competitiveness and improving domestic fundamentals that are supportive of least costly non-debt creating flows, particularly foreign direct investment (Deepak Mohanthy 2012).

1.7.3 FDI AND EXPORTS

Exports are one of the oldest forms of economic transfer and occur on a large scale between nations that have fewer restrictions on trade such as tariffs or subsidies. When a country specialises in the production of a few goods due to international trade and division of labour, it exports those commodities which it produces cheaper in exchange for what others can produce at a lower cost. It gains from trade and there is increase in national income which, in turn, raises the level of output and the growth rate of economy. Thus the higher level of output through trade tends to break the vicious circle of poverty and promotes economic development (Jhingan1995).
The ability to export goods helps an economy to grow by selling more overall goods and services. In a globalising world export success can serve as a measure for the competitiveness of a country’s industries. The export success among developing countries has been concentrated only in a few countries. But the comparative advantage of most of the developing countries still lies traditionally in primary commodities and unskilled-labour-intensive manufactures. In the long run, as they grow and accumulate capital and skills, wages increases and their competitive base has to change. They have to upgrade their primary and labour intensive exports into higher value-added items and they have to move into new, more advanced, export-oriented activities. All these activities can be obtained by improving and deepening the capabilities of domestic enterprises or by attracting foreign direct investment into export activities and upgrading these activities over time (Prasanna 2010). So FDI act as an important engine for export promotion.

FDI is expected to affect export from the supply side of the host country. FDI may enhance export-oriented productivity that may further improve export performance. Export contributes to growth by facilitating labour mobilization and capital accumulation. Firms tend to learn advanced technologies through exports and must adopt them to compete in the foreign marketplace. And the expansion in production resulting from exports reduces unit cost of production and increases productivity. In addition exports also provide a county with foreign exchange,
which is often scarce in the early stages of economic development, enabling a
country to import capital and intermediate goods. Increase in productivity
improves a country’s international competitiveness in price and quality, and
thereby boosts its exports (Jayakumar et. al. 2014).

Exports in India averaged US $ 3867.22 million from 1957 until 2014,
reaching an all-time high of US $ 30849.65 million in March of 2013 and a record
low of US $ 50.01 million in June of 1958. India’s main exports are engineering
goods (19 per cent of total exports), gems and jewellery (15 per cent), Chemicals
(13 per cent), agricultural products (9 per cent) and textiles (9 per cent). India is
also one of Asia’s largest refined product exporters with petroleum accounting for
around 18 per cent of total exports. India’s main export partners are United Arab
Emirates (12 per cent of total exports) and United States (11 percent). Others
include China, Singapore, Hong Kong and Netherlands (Makesh Kumar 2014).

Foreign direct investment not only provides an initial capital inflow, which
assists in the balance of payment of the host country, it is also an important mean
of obtaining capital, technology, skilled management, improved marketing know-
how and outlets for non-traditional exports. In addition a country’s economic
growth and FDI are closely linked with international trade. Economic growth,
whether in the form of export promoting or import substituting strategy, can
significantly affect trade flows. On the other hand expansion of exports can
promote economic growth by expanding the market size for developing countries.
It is understood that the objectives of multinational companies to invest in less developed countries is to reduce their cost of production in order to compete in neighbouring countries. This can increase exports of the host country. So it is evident that FDI, growth and international trade are mutually dependent on one another (Arshad and Muhammad 2012).

1.7.4 FDI AND IMPORTS

Mere increase in the value of imports and exports is not an indicator of the level of economic development of the country. It is the composition of trade that plays more important in an economy. The types of goods imported and exported by a country reveal whether a country is industrialized or backward. The changes occurring in the composition of trade over the years also show the economic transformation of a country. In the field of consumer goods, India primarily imports cereals and cereal preparations. The imports of raw materials and intermediate manufactures have been on the increase with development. The largest increase in the value of imports has occurred in petroleum oil and lubricants (Jhingan 1995).

FDI both at the initial investment and operation phases can influence import of a country. At the initial investment phase, import of equipments, machineries, installation facilities and experts all contribute to increased import balance. In the later phases of the investment, input nature, output type, productivity spill-over and type of relationship with other role players in the
industry determine the direction of effect of FDI on import of a country. Increased imports of consumer products encourage domestic import-substituting firms to innovate and restructure themselves in order to compete with foreign rivals (Jayakumar et. al. 2014).

1.8 STATEMENT OF THE PROBLEM

The economic reforms and policy changes undertaken by the government in 1991 brought a revolutionary change in the Indian economy. After the announcement of New Economic and liberalized Policy in the year 1991, foreign direct investment plays a vital role in the economic development of India. Foreign direct investment is used as a source of investment, described as source of economic growth and development that triggers technology and knowledge spillovers, contribute to international trade and commerce by enhancing exports in particular and improves the production efficiency of the host country. FDI not only affects the domestic investment climate but also influences foreign trade by import and export of goods and services. It is noted that FDI inflows are integral part of capital account of India’s balance of payments and FDI and current account are co-integrated in the long run. And also there have been many arguments stating that inflows of FDI improves the economic growth and consequently enhances employment opportunities. Therefore, the focus of this study is to analyse the inflows of foreign direct investment and its impact on GDP, on balance of payments, on exports and imports in the long run.
1.9 Objectives of the Study

1. To examine the trend and pattern of FDI in India during the post globalisation period.
2. To find out the contribution of FDI to India’s GDP.
3. To analyse the impact of FDI on India’s balance of payments position.
4. To understand the impact of FDI on India’s exports.
5. To know the impact of FDI on India’s imports.

1.10 Hypothesis

1. Foreign Direct Investment does not have a significant impact on Gross Domestic Product.
2. There is no association between FDI and India’s current account, capital account and overall balance in the balance of payments.
3. Foreign Direct Investment does not have any impact on India’s exports and imports.

1.11 IMPORTANCE OF THE STUDY

The study attempts to analyse the important dimensions of FDI in India. The study works out on the pattern and trends of foreign direct investment inflows in India. The study also examines the role of FDI on economic growth of India, balance of payments position, imports and exports of India for the period of 1991 to 2017.
1.12 METHODOLOGY

In this section the data source, period of study, analytical tools used for the present study are clearly depicted.

1.12.1 DATA SOURCE

The present study is entirely based on secondary data which is collected from Reserve bank of India annual report, Reserve bank of India bulletin, handbook of Statistics on Indian Economy and Economic Survey of various years.

1.12.2 PERIOD OF THE STUDY

The main objective of the study is to analyse the impact of Foreign Direct Investment in the post globalization era. In order to analyse the impact of FDI on GDP, imports, exports and balance of payments in the post globalization period, the data are collected for the period of 26 years from 1991 to 2017.

1.12.3 ANALYTICAL TOOLS

After collecting the data, the data are analysed and the results are interpreted. In order to analyse the collected data, the following statistical tools such as tables, percentages, averages, graphs, trend line are used.
1. To work out the annual growth rate the following formula is used.

\[ AGR = \frac{(X_2 - X_1)}{X_1} \]

Where, \( X_1 \) = first value of variable X,
\( X_2 \) = second value of variable X.

2. To find the trend in total FDI inflows and route wise FDI inflows trend analysis is worked out by using the following formula:

\[ Y = a + bx \]

Where, \( y \) = predicted value of the dependent variable
\( a \) = \( y \) axis intercept,
\( b \) = slope of the regression line (or the rate of Change in \( y \) for a given change in \( x \))
\( x \) = independent variable

As per the objectives, GDP, Current account, capital account, Exports, and Imports are taken as dependent variable and FDI as independent variable. The relationship between the independent variable FDI and other dependent variables is judged with the help of simple regression model.

1.13 LIMITATIONS OF THE STUDY

The statistical tools which are used in the present will have their own limitations.

\[ \text{v} \] The present study only covers the time period between 1991 and 2017.
The study has taken FDI inflows as independent variable and GDP, imports, exports and balance of payments as dependent variables. Many factors may be influential in determining these dependent variables selected for study. But the present study considers only FDI and the impact it creates on these dependent variables.

The researcher has collected the data from the RBI bulletins, RBI annual reports and handbook of statistics on Indian Economy. So there may be variations in the collected data from other sources due to the different way of calculations.

The study of FDI inflows countrywise is done selecting only the top ten investing countries.

The impact of FDI in the state level could have been included but due to time and data constraints this work has been restricted only to the total FDI inflows into India.

1.14 CONCEPTS USED IN THIS STUDY

Foreign Direct Investment (FDI)

Foreign Direct Investment refers to the net inflows of investment to acquire a lasting management interest in an enterprise operating in an economy other than that of the investor.
Gross Domestic Product (GDP)

GDP is the monetary value of all final goods and services produced by all the people within a domestic territory during an accounting year.

GDP = C + I + G + (X - M)

Where C = Consumption expenditure, I = Investment expenditure,

G = Government expenditure, X = Exports and M = Imports.

Exports

A function of international trade whereby goods produced in one country are shipped to another country for future sale or trade.

Imports

A function of international trade whereby goods or services are brought into one country from another country.

Current Account

Current account of a country consists of all transactions relating to trade in goods and services and unilateral transfers. Service transactions include travel and transportation, income and payments on foreign investments, etc.
Capital Account

Capital account of a country consists of its transactions in financial assets in the form of short-term and long-term lending and borrowings, and private and official investments.

1.15 PLAN OF THE STUDY

The study contains five chapters. The first chapter gives a brief introduction of foreign direct Investment, and the impact it creates on economic variables such as GDP, balance of payments, exports and imports. This chapter also provides information about the FDI inflows at the world level, to the developing countries and to the developed countries. This chapter also presents the statement of the problem, objectives, hypothesis, methodology, period of the study, importance, scope of the study and limitations.

The second chapter presents the review of literature. In this chapter the studies of various authors are reviewed under the headings FDI inflows, impact of FDI on GDP, impact of FDI on balance of payments, and impact of FDI on exports and imports. A total of ninety six studies were reviewed from journals, newspapers and books by the researcher. This chapter also connects the study with the existing theories.

The third chapter gives the detailed analysis of total FDI inflows into India, country wise FDI inflows and sector wise FDI inflows.
The fourth chapter analyses the impact of FDI on selected economic variables such as GDP, balance of payments, exports and imports. The formulated hypotheses are also tested in this chapter.

The fifth chapter presents the findings of the study, suggestions and the conclusion.