



## **An analytical study on India's Foreign Direct Investment**

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### **Abstract**

India is a country that has been able to restore investor confidence in its markets, even during the toughest of times. Increase in capital flows, foreign direct investments (FDI) and overseas entities' participation reflect the fact that Indian markets have fared well in recent times. Moreover, foreign companies are viewing the South-Asian nation as a strategic hub for their operations and investments owing to investor-friendly policy environment, positive ecosystem and huge potential for growth. Indian Incorporation's increasing presence over the global canvas and Indian Government's consistent support to the FDI space has facilitated remarkable developments as India's strength is in its information base. This paper brings out an analysis on the foreign direct investments year-wise total inflows, sector wise inflows, top 10 contributing countries to India's investment inflows and total FDI outflows, to make an assessment on growth rate, identifying the major setbacks and loopholes that allows foreign institutions to enter our nation.

**KEYWORDS:** FDI, FDI inflows, FDI outflows, Growth, International Finance

### **INTRODUCTION TO THE STUDY**

#### **FOREIGN DIRECT INVESTMENTS**

FDI is nothing but "an investment made by a company or entity based in one country, into a company or entity based in another country". Foreign direct investments differ substantially from indirect investments such as portfolio flows, wherein overseas institutions invest in equities listed on a nation's stock exchange. Entities making direct investments have a significant degree of influence and control over the company into which the investment is made.

#### **DEFINITION**

According to **the International Monetary Fund**, foreign direct investment, commonly known as FDI,

"... refers to an investment made to acquire lasting or long-term interest in enterprises operating outside of the economy of the investor."



## **HISTORICAL INSIGHT**

According to history the United States was the leader in the FDI activity dating back as far as the end of World War II. Businesses from other nations have taken up the flag of FDI, including many who were not in a financial position to do so just a few years ago.

The practice has grown significantly in the last couple of decades, to the point that FDI has generated quite a bit of opposition from groups such as labor unions. These organizations have expressed concern that investing at such a level in another country eliminates jobs. Legislation was introduced in the early 1970s that would have put an end to the tax incentives of FDI. But members of the Nixon administration, Congress and Business Interests rallied to make sure that this attack on their expansion plans was not successful.

One key to understanding FDI is to get a mental picture of the global scale of corporations able to make such investment. A carefully planned FDI can provide a huge new market for the company, perhaps introducing products and services to an area where they have never been available. Not only that, but such an investment may also be more profitable if construction costs and labor costs are less in the host country.

FDI growth has been a key factor in the “international” nature of business that many are familiar with in the 21st century. This growth has been facilitated by changes in regulations both in the originating country and in the country where the new installation is to be built.

Corporations from some of the countries that lead the world’s economy have found fertile soil for FDI in nations where commercial development was limited, if it existed at all. The dollars invested in such developing-country projects increased 40 times over in less than 30 years.

## **FOREIGN DIRECT INVESTMENT IN INDIA**

Foreign investment was introduced in 1991 under Foreign Exchange Management Act (FEMA), driven by Finance Minister Manmohan Singh. As Singh subsequently became a Prime Minister, this has been one of his top political problems, even in the 2012 election. India disallowed overseas corporate bodies (OCB) to invest in India.

Starting from a baseline of less than \$1 billion in 1990, a recent UNCTAD survey projected India as the second most important FDI destination (after China) for transnational corporations during 2010–2012. As per the data, the sectors that attracted higher inflows were services, telecommunication, construction activities and computer software and hardware. Mauritius, Singapore, US and UK were among the leading sources of FDI. Based on UNCTAD data FDI flows were \$10.4 billion, a drop of 43% from the first half of the last year.

## **METHODS**

The foreign direct investor may acquire voting power of an enterprise in an economy through any of the following methods:

- by incorporating a wholly owned subsidiary or company anywhere
- by acquiring shares in an associated enterprise



- through a merger or an acquisition of an unrelated enterprise
- participating in an equity joint venture with another investor or enterprise

#### **COUNTRIES SENDING FDI TO INDIA ARE:**

- Mauritius
- U.K
- U.S.A
- France
- Malaysia
- Singapore
- Japan
- Germany
- Netherlands

#### **SECTORS IN INDIA ATTRACTING FDI FROM FOREIGN COUNTRIES ARE:**

- Telecommunications that includes services of cellular mobile, radio paging, and basic telephone
- Chemicals
- Metallurgical industries
- Food processing industries
- Pharmaceuticals and drugs
- Fuels
- Electrical equipment that includes electronics and computer software
- Services sector that includes financial and non-financial

#### **FOREIGN DIRECT INVESTMENT POLICY**

India's foreign investment policy has been formulated with a view to inviting and encouraging FDI into India. The process of regulation and approval has been substantially liberalised. FDI under automatic route is permitted in most activities/sectors, except a few where prior approval of the Government is required.

Government of India welcomes FDI in all sectors where it is permitted, especially for development of infrastructure, technological upgradation of Indian industry through 'greenfield' investments and in projects having the potential of creating employment opportunities on a large scale. Investment for setting up Special Economic Zones (SEZs) and establishing manufacturing units are also welcomed.

#### **REVIEW OF LITERATURE:**

- ✚ **Shalini Aggarwal, Ankush Singla and Ritu Aggarwal (Sep 2012)**, studied on the need of FDI in India, to exhibit the sector-wise & year-wise analysis of FDI's in India and to rank the sectors based upon highest FDI inflows. The results show that Mauritius is the country that has invested highly in India followed by Singapore, Japan, and USA. It has also showed that there has been a tremendous increase in FDI inflow in India during the year 2000 to 2011.



- ✚ According to the article published on topic “**FDI inflows decline by over 65% in April – June period**” in **Business today** dated **August 11, 2012** , FDI inflows were \$13.4 billion in April-June 2011-12 period and as per Reserve Bank of India (RBI), the FDI inflow in the country was \$1.32 billion in June as against \$5.73 billion in the same month last year. The data also revealed that the net FDI -- difference between FDI inflow and outflow -- plunged 58 per cent to USD 3.83 billion in the first three months of the fiscal. The net FDI inflow was USD 9.04 billion in the same period of 2011-12.
- ✚ **Ms. Parul Mittal; Mr. Sandeep Aggarwal (July 2012)** made a general analysis of the inflows and outflows of FDI since the post liberalization era. The purpose of this paper was to provide an examination of foreign direct investment in various sectors. At the end of this examination, figures showed the trend of FDI inflows and FII in India and geographical distribution of FDI.
- ✚ **Partha Sinha (May, 2012)**, on Record FDI outflows Report stated to TOI that Domestic uncertainties like policy flip-flops, combined with global risk aversion, is prompting foreign companies to increasingly repatriate their investments, categorized as foreign direct investment (FDI), out of India during the last three years ended December 2011. "FDI into India has risen exponentially since the 2000s. However, over the last three years some of this money is being repatriated," Global deleveraging had forced companies to sell their Indian assets and repatriate funds to their home country.
- ✚ According to **Dr. Patil Usha.N (February 2012)**, there were varied viewpoints on the impact of FDI in the retail sector in India, According to one viewpoint, the US evidence is empirical proof to the fact that FDI in the retail sector does not lead to any collapse in the existing employment opportunities. The unorganized retail sector contributes about 14% to the GDP and absorbs about 7% of our labour force. Hence the issue of displacement of labour consequent to FDI is of primal importance.
- ✚ **K.S. ChalapatiRao and BiswajitDhar (February 2011)** made an attempt on the ambiguities surrounding the definition and the non-adherence of international norms in measuring the FDI inflows. The study found that portfolio investors and round tripping investments have been important contributors to India’s reported FDI inflows thus blurring the distinction between direct and portfolio investors on one hand and foreign and domestic investors on the other. These investors were also the ones which have exploited the tax haven route most.
- ✚ **Ravi Subramanian, CharuSachdeva, Sebastian Morris (March 2010)**: discussed on trends in India's outward FDI over the last decade and attempts to identify the driving factors for the same. The aim of the study was to provide policy makers with insights regarding levers which would help in encouraging FDI outflows and to stimulate further research in foreign investment from emerging economies. The paper also discussed the key policy changes that impacted outward FDI from India in the last decade and relationship of outward FDI with other macroeconomic indicators such as GDP and Fischer Open Differential.



- ✦ **Sasidaran Gopalan and Ramkishen S. Rajan (June 2009)**, analyzed that the rise of India has led to both as source and host of FDI to generate a sizeable literature on the determinants and characteristics of inflows and outflows at an aggregate level

### OBJECTIVE OF THE STUDY

- ❖ To study the growth of total FDI inflows and outflows in India for the past 10 year period.
- ❖ To analyze the top investing countries and sectors in FDI inflows in India.

### LIMITATIONS OF THE STUDY

The study on country and sector wise inflows is made only for the past 3 year period accounting to the financial year 2010 - 2013 (up to Jan 2013).

### RESEARCH METHODOLOGY

This research is descriptive in nature. The data is secondary in nature. Graphs and tables have also been used where ever required to depict statistical data of FDI during the study period.

Secondary data used:

- Reports and publications of various associations connected with business and Industry, Agencies, government etc.
- Websites of RBI, DIPP, OECD.
- Journals, books and magazines related to FDI in different sector
- Historical documents and other sources of published information.

### ANALYSIS AND DISCUSSION

Table 1: DIPP'S – FINANCIAL YEAR-WISE FDI EQUITY INFLOWS IN INDIA

Year	Amount In Crores	Amount In USD Million	% Growth	Cumulative % Growth
2003-04	10,064	2,188	(-)19%	(-)19%
2004-05	14,653	3,219	47%	28%
2005-06	24,584	5,540	72%	100%
2006-07	56,390	12,492	125%	226%
2007-08	98,642	24,575	97%	322%
2008-09	142,829	31,396	28%	350%
2009-10 #	123,120	25,834	(-)18%	332%



2010-11 #	97,320	21383	(-)17%	315%
2011-12 # ^	165,146	35,121	64%	379%
2012-13 # (UP TO Jan 2013)	103,956	19,103		

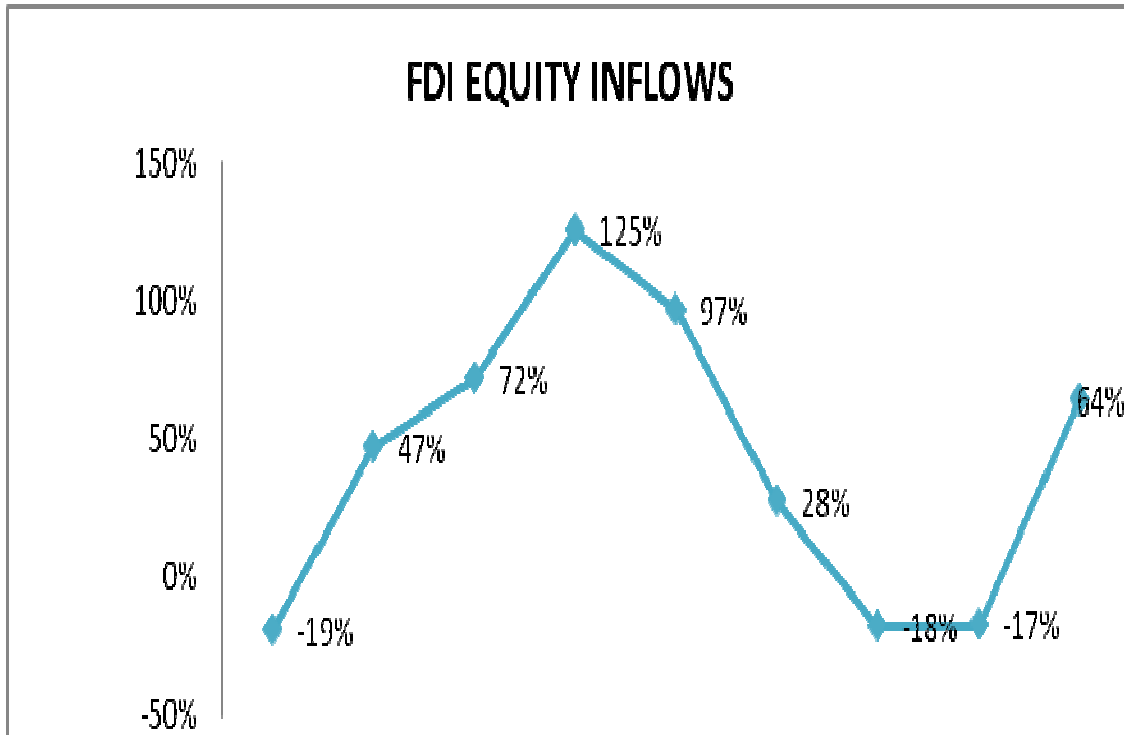
Note: FEDAI (Foreign Exchange Dealers Association of India) conversion rate from rupees to US dollar applied, on the basis of monthly average rate provided by RBI (DEPR), Mumbai.# Figures for the years 2009 to 13 are provisional subject to reconciliation with RBI. ^ Inflows for the month of March, 2012 are as reported by RBI, consequent to the adjustment made in the figures of Mar, Aug, and Oct,11.

Source: As per DIPP’s FDI data base

**Interpretation:**

It shows that the total amount of FDI inflows in India during the last 10 years i.e 2003 to 2013. The FDI inflow for the year 2003-04 is at 10,064 crore rupees. In 2008-09 there was a huge investment in FDI in 142,829 crore Rupees and started to dip by 18% and 19% in 2009-10 and 2010-11. After that the FDI inflows has started to gain its momentum. So it can be said that the foreign investment have been on rise in India.

**Chart 1:DIPP’S – FINANCIAL YEAR-WISE FDI EQUITY INFLOWS IN INDIA**



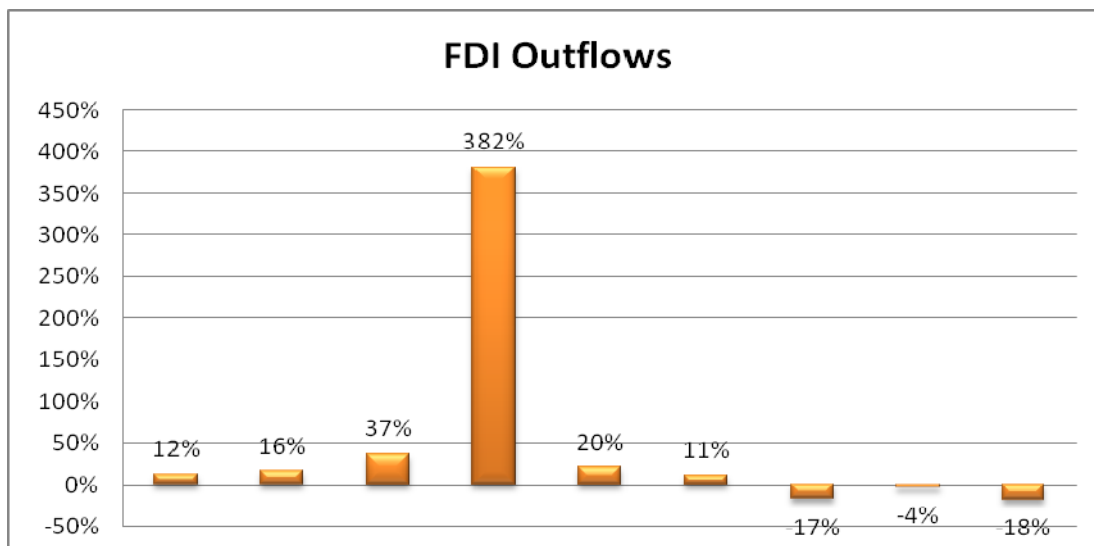
**Table 2: TOTAL FDI OUTFLOWS FOR THE PERIOD 2002-2012 (IN US \$ MN)**

Year	Amount in USD million	%age growth	Cumulative %age
2002-03	1,679	...	...
2003-04	1,879	12%	12%
2004-05	2,179	16%	28%
2005-06	2,978	37%	65%
2006-07	14,344	382%	446%
2007-08	17,281	20%	467%
2008-09	19,257	11%	478%
2009-10	15,928	-17%	461%
2010-11	15,346	-4%	457%
2011-12 (P)	12,608	-18%	439%

Source: OECD Fact book: Economic, Environmental and Social Statistics; (P) - Provisional

Interpretation:

It shows that the amount of total FDI outflows for the period 2002 to 2012 and the highest FDI outflows in the country is the period 2006-07 with 14,344 in US \$ mn from 2,978 USD mn in 2005-06. The succeeding periods show constant fluctuations.

**Chart 2: TOTAL FDI OUTFLOWS FOR THE PERIOD 2002-2012 (IN US \$ MN)**

**Table 3: TOTAL FDI INFLOWS FOR THE PERIOD 2003-2013 (IN US \$ MN)**

Year	Amount in USD Million	% Growth	Cumulative % Growth
2003-04	4,322	(-)14%	-14%
2004-05	6,051	40%	26%
2005-06	8,961	48%	74%
2006-07	22,826	155%	229%
2007-08	34,843	53%	281%
2008-09	41,873	20%	301%
2009-10 (P) (+)	37,745	(-)10%	292%
2010-2011 (P) (+)	34,847	(-)8%	284%
2011-12 (P)	46,553	34%	318%
2012-13 (P) (UP TO Jan 2013)	30,824		

Source: As Per DIPP's FDI Database.

RBI s Bulletin March, 2013 dt. 11.03.2013 (Table No. 34 – FOREIGN INVESTMENT INFLOWS). Figures updated by RBI up to January, 2013.

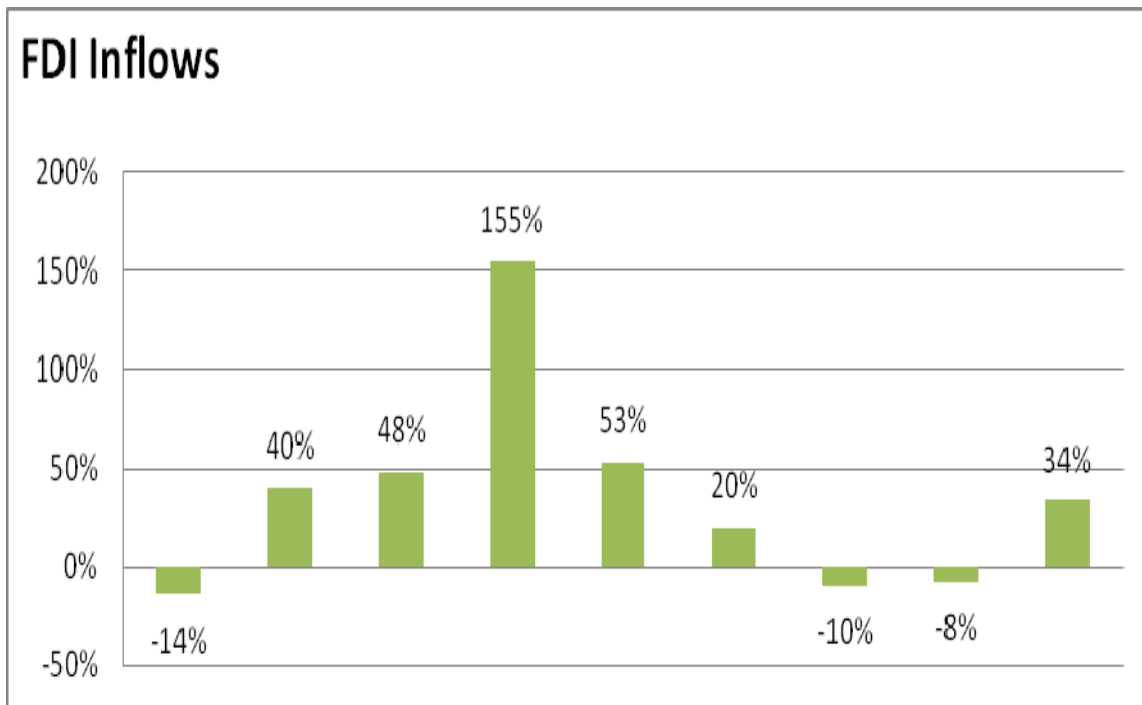
(P) All figures are provisional. “+” Data in respect of „Re-invested earnings & „Other capital for the years 2009- 10, 2010-11 & 2012-13 are estimated as average of previous two years.

Interpretation:

It shows that the highest amount of FDI inflows was in the period 2011 -12 with a recovery after the recession period showing a dip of -10% during the year 2009-10 and 2010-11 (-8%). i.e. 46,553 in US \$ mn.



**Chart 3: TOTAL FDI INFLOWS FOR THE PERIOD 2003-2013 (IN US \$ MN)**



**Table 4: SECTORS ATTRACTING HIGHEST FDI EQUITY INFLOWS IN INDIA**

Amount in Rs. Crores (US\$ in millions)

Ranks	Sector	2010-11 (April - March)	2011-12 ( April - March)	2012-13 (April – Jan.)	Cumulative Inflows	% age to total Inflows (In terms of US\$)
1.	SERVICES SECTOR **	15,054 (3,296)	24,656 (5,216)	25,367 (4,660)	171,345 (37,063)	20 %
2.	CONSTRUCTION DEVELOPMENT: TOWNSHIPS, HOUSING, BUILT-UP INFRASTRUCTURE	7,590 (1,663)	15,236 (3,141)	6,562 (1,206)	100,363 (21,954)	12 %
3.	TELECOMMUNICATIONS (radio paging, cellular mobile, basic telephone services)	7,542 (1,665)	9,012 (1,997)	507 (93)	57,585 (12,645)	7 %
4.	COMPUTER SOFTWARE & HARDWARE	3,551 (780)	3,804 (796)	2,382 (435)	52,500 (11,640)	6 %
5.	DRUGS &	961	14,605	5,389	48,257	5 %



	PHARMACEUTICALS	(209)	(3,232)	(1,008)	(10,202)	
6.	CHEMICALS (OTHER THAN FERTILIZERS)	10,612 (2,354)	18,422 (4,041)	1,466 (268)	40,366 (8,857)	5 %
7.	POWER	5,796 (1,272)	7,678 (1,652)	2,871 (526)	36,085 (7,825)	4 %
8.	AUTOMOBILE INDUSTRY	5,864 (1,299)	4,347 (923)	4,916 (895)	35,702 (7,653)	4 %
9.	METALLURGICAL INDUSTRIES	5,023 (1,098)	8,348 (1,786)	7,439 (1,385)	34,375 (7,426)	4 %
10	HOTEL & TOURISM	1,405 (308)	4,754 (993)	17,401 (3,190)	32,884 (6,562)	4 %

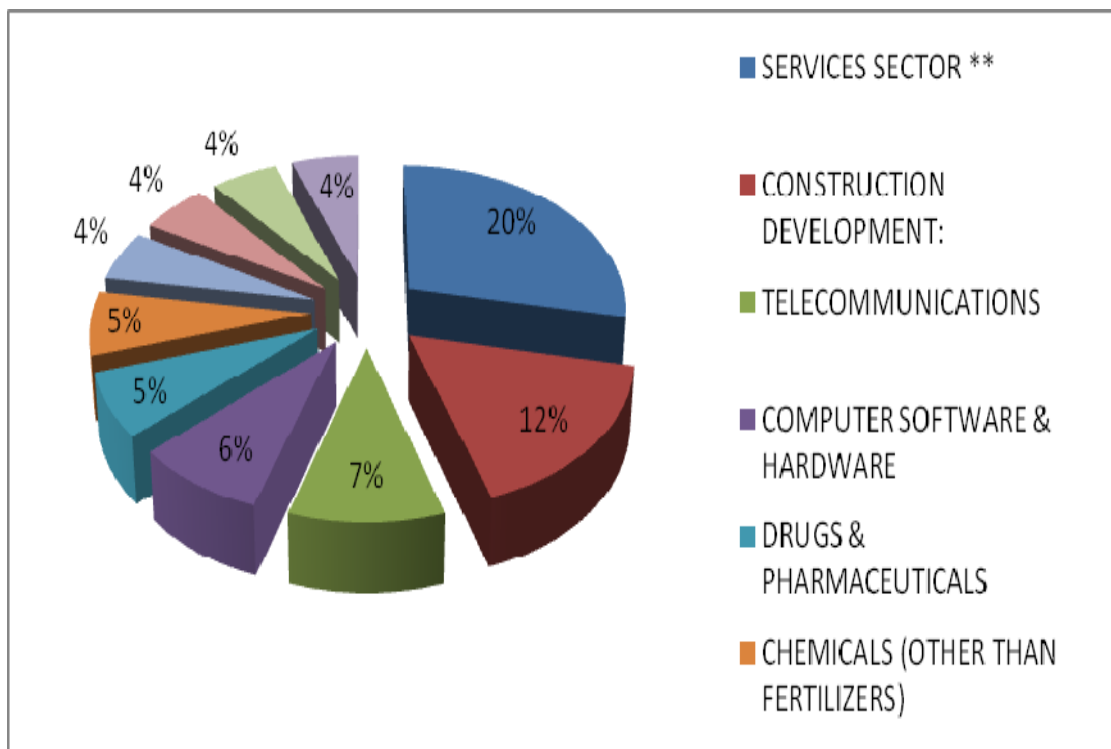
Source: As per DIPP’s FDI data base

Note: (i) \*\* Services sector includes Financial, Banking, Insurance, Non-Financial / Business, Outsourcing, R&D, Courier, Tech. Testing and Analysis

Interpretation:

According to the table Service sector is with highest FDI inflow of 20%, after which the next follows the construction development and Telecommunication sector with 12% and 7%.

**Chart 4: SECTORS ATTRACTING HIGHEST FDI EQUITY INFLOWS IN INDIA**



**Table 5: STATEMENT ON COUNTRY-WISE FDI INFLOWS**

Amount in Rs. crores (US\$ in millions)

<b>Ranks</b>	<b>Country</b>	<b>2010-11</b> (April - March)	<b>2011-12</b> ( April - March)	<b>2012-13</b> (April – Jan.)	<b>Cumulative</b> <b>Inflows</b>	<b>%age to</b> <b>total</b> <b>Inflows</b> <b>(in terms</b> <b>of US \$)</b>
1.	MAURITIUS	31,855 <b>(6,987)</b>	46,710 <b>(9,942)</b>	44,508 <b>(8,175)</b>	333,979 <b>(72,343)</b>	<b>38 %</b>
2.	SINGAPORE	7,730 <b>(1,705)</b>	24,712 <b>(5,257)</b>	9,968 <b>(1,823)</b>	87,556 <b>(18,976)</b>	<b>10 %</b>
3.	U.K.	12,235 <b>(2,711)</b>	36,428 <b>(7,874)</b>	5,625 <b>(1,048)</b>	80,286 <b>(17,517)</b>	<b>9 %</b>
4.	JAPAN	7,063 <b>(1,562)</b>	14,089 <b>(2,972)</b>	9,308 <b>(1,693)</b>	67,159 <b>(14,006)</b>	<b>7 %</b>
5.	U.S.A.	5,353 <b>(1,170)</b>	5,347 <b>(1,115)</b>	2,726 <b>(500)</b>	50,615 <b>(11,064)</b>	<b>6 %</b>
6.	NETHERLANDS	5,501 <b>(1,213)</b>	6,698 <b>(1,409)</b>	8,219 <b>(1,517)</b>	40,544 <b>(8,626)</b>	<b>5 %</b>
7.	CYPRUS	4,171 <b>(913)</b>	7,722 <b>(1,587)</b>	2,365 <b>(435)</b>	32,035 <b>(6,835)</b>	<b>4 %</b>
8.	GERMANY	908 <b>(200)</b>	7,452 <b>(1,622)</b>	3,204 <b>(587)</b>	24,032 <b>(5,208)</b>	<b>3 %</b>
9	FRANCE	3,349 <b>(734)</b>	3,110 <b>(663)</b>	3,159 <b>(585)</b>	16,536 <b>(3,512)</b>	<b>2 %</b>
10.	U.A.E.	1,569 <b>(341)</b>	1,728 <b>(353)</b>	940 <b>(171)</b>	11,260 <b>(2,414)</b>	<b>1 %</b>

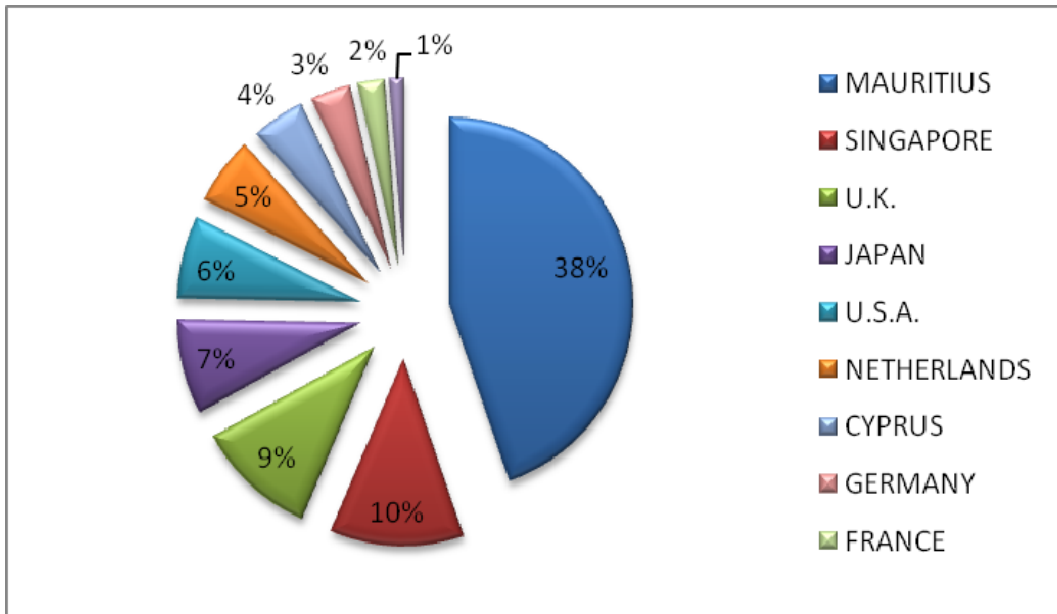
Source: As per DIPP's FDI data base

**Interpretation:**

The report shows that the MAURITIUS country is the highest foreign investor in India with 38%. After Mauritius, Singapore and UK invest the highest FDI in India with 10% and 9% respectively and Japan with 4th position in FDI in India.



**Chart 5: STATEMENT ON COUNTRY-WISE FDI INFLOWS**



**FINDINGS**

- The study shows that the inflows and outflows are constantly performing well in terms of growth with a tremendous growth after the recession period.
- It also depicts that Service Sector plays a major role with regard to foreign direct investments acting as a priority sector in investment and Construction development being second shows much scalability of improvement in FDI policy reforms. Mauritius and Singapore ranks the top in investing countries with maximum FDI inflows year after year.

**CONCLUSION**

It can be concluded that despite the Indian Government’s closed FDI policies the FDI equity inflows shows that India’s long-term outlook is strong, though in the short term, there is some erosion of confidence, which is visible in the outflows and about 57% of foreign investments are from Mauritius, Singapore and Japan. It also shows that FDI has helped to raise the output, productivity and employment in service sector as the Indian service sector generates employment opportunities. Next to it Infrastructure and Telecommunications helps in strengthening the Indian economic condition. Hence it can be said that the Government’s intention to attract foreign institutional investors as a way to halt the rupees’ depreciation puts short-term stagnation in FDI and helps country to make an impression on the world wide level through liberalization and globalization, paving way to retail sector.



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