# FDI IN INDIA

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## ABSTRACT

Foreign direct investment (FDI) is direct investment by a company in production located in another country either by buying a company in the country or by expanding operations of an existing business in the country. No doubt, FDI plays a crucial role in enhancing the economic growth and development of the country. Moreover, FDI as a strategic component of investment is needed by India for achieving the objectives of its second generation of economic reforms and maintaining this pace of growth and development of the economy. The main objective of this paper is to showing the trends of FDI in India and its threats and opportunity in Indian economy. And the trend of FDI in second decade of liberalization is greatly satisfactory. The crucial test for India is to move the FDI to a consistent upward trend. Although India is not the most preferred destination of global FDI, but there has been a generous flow of FDI in India since 1991. It has become the 2nd fastest growing economy of the world. The economic reform process started in 1991 helps in creating a conducive and healthy atmosphere for foreign investors and thus, resulting in substantial amount of FDI inflows in the country. 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. In fact, in the early nineties, Indian economy faced severe Balance of Payment crisis. Exports began to experience serious difficulties. In 1990-91 we adopted New Economic Policy. Then India opens its door to FDI inflows and adopted a more liberal foreign policy in order to restore the confidence of foreign investors. A large number of changes that were introduced in the country's regulatory economic policies heralded the liberalization era of the FDI policy regime in India and brought about a structural breakthrough in the volume of the FDI .

**Key word: FDI, Inflows, Outflows.**

## INTRODUCTION

Foreign direct investment (FDI) is a direct investment into production or business in a country by an individual or company of another country, either by buying a company in the target country or by expanding operations of an existing business in that country. Foreign direct investment is in contrast to portfolio investment which is a passive investment in the securities of another country such as stocks and bonds. One of the most striking developments during the last two decades is the remarkable growth of FDI in the global economic landscape. This unprecedented growth of global economic landscape

FDI in 1990 around the world make FDI an important and vital component of development strategy in both developed and developing nations and policies are designed in order to stimulate inward flows. In fact, FDI provides a win – win situation to the host and the home countries. Both countries are directly interested in inviting FDI, because they benefit a lot from such type of investment. The 'home' countries want to take the advantage of the vast markets opened by industrial growth. On the other hand, the 'host' countries want to acquire technological and managerial skills and supplement domestic savings and foreign exchange. Moreover, the paucity of all types of resources viz. financial, capital, entrepreneurship, technological know- how, skills and practices, access to markets- abroad- in their economic development, developing nations accepted FDI as a sole visible panacea for all their scarcities. Further, the integration of global financial markets paves ways to this explosive growth of FDI around the globe.

### MEANING

Foreign direct investment (FDI) is direct investment by a company in production located in another country either by buying a company in the country or by expanding operations of an existing business in the country. Foreign direct investment is done for many reasons including to take advantage of cheaper wages in the country, special investment privileges such as tax exemptions offered by the country as an incentive to gain tariff-free access to the markets of the country or the region.

## OBJECTIVE

- To introduce and analyze FDI in India.

## FDI IN INDIA

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. However, researchers could not portray the complete history of FDI pouring in India due to lack of abundant and authentic data. Before independence major amount of FDI came from the British companies. British companies' setup their units in mining sector and in those sectors that suits their own economic and business interest. After Second World War, Japanese companies entered Indian market and enhanced their trade with India, yet U.K. remained the most dominant investor in India. Further, after Independence issues relating to foreign capital, operations of MNCs, gained attention of the policy makers. Keeping in mind the national interests the policy makers designed the FDI policy which aims FDI as a medium for acquiring advanced technology and to mobilize foreign exchange resources. The first Prime Minister of India considered foreign investment as "necessary" not only to supplement domestic capital but also to secure scientific, technical, and industrial knowledge and capital equipment. With time and as per economic and political regimes there have been changes in the FDI policy too.

The industrial policy of1956, allowed MNCs to venture through technical collaboration in India. However, the country faced two severe crisis in the form of foreign exchange and financial resource mobilization during the second five year plan . Therefore, the government adopted a liberal attitude by allowing more frequent equity participation to foreign enterprises, and to accept equity capital in technical collaborations. The government also provided many incentives such as tax concessions, simplification of licensing procedures and de- reserving some industries such as drugs, aluminum, heavy electrical equipment, fertilizers, etc. in order to further boost the FDI inflows in the country. This liberal attitude of government towards foreign capital lures investors from other advanced countries like USA, Japan, and Germany etc. But due to significant outflow of foreign reserves in the form of remittances of dividends, profits, royalties etc., the government has to adopt strict policy inIndia.In startingperiod, the government adopted a selective and highly restrictive foreign policy, type of FDI and ownerships of foreign companies was concerned. Government setup Foreign Investment Board and enacted Foreign Exchange Regulation Act in order to regulate flow of foreign capital and FDI flow to India. The soaring oil prices continued low exports and policy as far as foreign capital deterioration in Balance of Payment position during 1980s forced the government to make necessary changes in the foreign policy. It is during this period the government encourages FDI, allow MNCs to operate in India.

India's economic reforms way back in 1991 has generated strong interest in foreign investors and turning India into one of the favorite destinations for global FDI flows.In fact, in the early nineties, Indian economy faced severe Balance of payment crisis. Exports began to experience serious difficulties. There was a marked increase in petroleum prices because of the gulf war. The crippling external debts were debilitating the economy. India was left with that much amount of foreign exchange reserves which can finance its three weeks of imports. The out flowing of foreign currency which was deposited by the Indian NRI's gave a further jolt to Indian economy. The overall Balance of Payment reached at Rs. (-) 4471 crores. Inflation reached at its highest level of 13%. Foreign reserves of the country stood at Rs.11416 crores. The continued political uncertainty in the country during this period adds further to worsen the situation. As a result, India's credit rating fell in the international market for both short- term and long-term borrowing. All these developments put the economy at that time on the edge of default in respect of external payments liability. In this critical face of Indian economy, then finance Minister of India Dr. Manmohan Singh with the help of World Bank and IMF introduced the macro – economic stabilization and structural adjustment program.

As a result of these reforms India open its door to FDI inflows and adopted a more liberal foreign policy in order to restore the confidence of foreign investors. Further, under the new foreign investment policy Government of India constituted FIPB (Foreign Investment Promotion Board) whose main function was to invite and facilitate foreign investment through single window system from the Prime Minister's Office. The foreign equity cap was raised to 51 percent for the existing companies. Government had allowed the use of foreign brand names for domestically produced products which was restricted earlier. India also became the member of MIGA (Multilateral Investment Guarantee Agency) for protection of foreign investments. Government lifted restrictions on the operations of MNCs by revising the FERA Act 1973. New sectors such as mining, banking, telecommunications, highway construction and management were open to foreign investors as well as to private sector.

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According to RBI, this reflected the continued strength of sustained economic activity and positive investment climate. The strength of the corporate performance, positive investor sentiments, and further liberalization of FDI policies in sectors such as telecom, retail and expanding permotitional efforts by the government played a role in attracting FDI.

## FDI - OPPORTUNITIES AND CHALLENGES

FDI have helped India to attain a financial stability and economic growth with the help of investment in different sectors.FDI has boosted the economic life of India. after new economic policy in India, there has been a positive growth rate in Indian economy. There is direct relationship between FDI and employment. FDI help in developing the economy by generating employment to the unemployed. Generating revenues in the form of taxes.

But FDI will continue, particularly in crucial sectors such as IT, telecom, financial and pharmaceuticals. These might be aided by trade liberalization, investment in capital markets, deregulation and the fiercer competitive pressures resulting from globalization and technological changes.Other motivations include efforts to attain a dominant market position as well as short-term financial gains in terms of stock value. In many instances the dynamics of the process feeds upon itself, as firms fear that if they do not find suitable partners, they may not survive, in the long run. From the host-country point of view, some important issues can be identified. To what extent can foreign investment serve the overall socio-economic goals in an open regime? Income disparities, employment generation, technology flows, environmental costs of industrial development, commitment to exports are some of the key issues.

There could be a crowding-out effect in the face of competition for scarce resources and markets. The pattern of investment and the routes FDI flows might take may undergo a significant change. There could be takeovers of local firms in a few cases with implications for domestic brands. Takeovers per se are not to be frowned upon. But the ground rules for transparency and prevention of insider-trading practices must be enforced vigorously under SEBI guideline. Today; this is a weak area in Indian corporate mergers. Improving the host country's negotiating power with TNCs needs attention. Information of cost and the status of technology offered and the global strategies of firms are vital to strengthen the bargaining capability.

There is likely to be an increasing role of the TNC home countries in controlling the flow of critical or dual technology on so called `security grounds' which issue musty be discussed to evolve suitable international standards. With particular reference to portfolio investments and profit return, host countries must evolve suitable financial policies and instruments to prevent capital market volatility.

This might also be true when more Indian companies have their stocks listed in world capital markets where the volumes traded are high as is the velocity. The solution is not to argue against these measures if we want globalization but to encourage industrialization and improve corporate performance to international standards. Also, the number of good scripts must increase as should the volumes traded. The regulatory framework of the capital market must also improve with the professionalization of brokerage firms, and the enforcement of strict dealing and settlement standards. Increasingly, trading velocity will be much higher and scripless trading, with networked stock markets to rope in more investors, will be necessary.

Importantly, economic management should not give cause for alarm as FIIs are highly temperamental investors whose business is to maximize profits and minimize risks for their members and not necessarily to work for the development of the host country. This must be done keeping the markets liberalized and open so that investor confidence is not shaken.

With increased investment by TNCs, there should be effective tools in our tax system and the administrative machinery needs to be adequately adjusted to address the question of transfer pricing. Lastly, evolving good corporate governance and proper internal checks and balances through independent audit committees is a must. So far, this area has been only a talking point among corporate with some leading chambers of commerce even treating this issue as a voluntary measure. Critics of FDI feel that liberalization would risk the unorganized retail sector and would adversely affect the small retailers, farmers and consumers and give rise to monopolies of large corporate houses which can adversely affect the pricing and availability of goods. They also contend that the retail sector in India is one of the major employment providers and permitting. FDI in this sector can displace the unorganized retailers leading to loss of livelihood.

So we can say, Foreign Direct Investment (FDI) as an important driver of growth. It is an important source of non-debt financial resources for country for economic development. Besides it is a means of achieving technical knowledge and employment generation of employment. However, many are of the view that FDI is a big threat to sovereignty of host and domestic business houses. Faster exploitation of natural resources for profit may deprive host from such resources in long run. Midst of debate on pros and cons of FDI, world economy has observed a phenomenal change in volume and pattern of FDI. There is clearly an intense global competition of FDI. India is not behind this global race of attracting foreign investment. India emerged as an attractive FDI destination in services but has failed to evolve a manufacturing hub which has greater economic benefit. FDI though one of the important sources of financing the economic development, but not is not a solution for poverty eradication, unemployment and other economic ills.

## CONCLUSION

Capital investment and human resources are the pivots of development of a country. FDI takes better technology, more employment and growth for economy with it. In the post liberalization age, India is able to achieve a huge amount of FDI in a variety of sectors, India's workforce of scientists, researchers, engineers, English-speaking people and democratic regime make it an attractive destination for FDI. And the trend of FDI in second decade of liberalization is greatly satisfactory. The crucial test for India is to move the FDI to a consistent upward trend. But, Critics of FDI feel that liberalization would jeopardize the unorganized retail sector and would adversely affect the small retailers, farmers and consumers and give rise to monopolies of large corporate houses which can adversely affect the pricing and availability of goods. They also contend that the retail sector in India is one of the major employment providers and permitting FDI in this sector can displace the unorganized retailers leading to loss of livelihood. Finally, it may be concluded that developing countries has make their presence felt in the economics of developed nations by receiving a descent amount of FDI in the last three decades. Although India is not the most preferred destination of global FDI, but there has been a generous flow of FDI in India since 1991. It has become the 2nd fastest growing economy of the world. The economic reform process started in 1991 helps in creating a conducive and healthy atmosphere for foreign investors and thus, resulting in substantial amount of FDI inflows in the country.

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