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IMPLICATIONS OF FDI IN INDIA

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ABSTRACT

In a number of cases, it is observed that FDI if brought in a particular sector; proves to be a boon for that particular sector. Hence, it can be said that FDI is good for the various sectors. Investment from the foreign industries and organizations provide better opportunities for the domestic industrial sectors where a good range of development can be observed.

The trend of FDI is increasing in India as government is promoting the level of FDI in various industrial sectors so that the level of loss in these sectors can be minimized. The introduction of FDI is also favoring the privatization in the government sectors. In this way, the government wants to provide reasonable growth in these sectors. Hence, it can be said that FDI is proving to be game changer in various private and public sectors. The current paper highlights the implications of FDI in India.

KEYWORDS:

FDI, Economy, Investment

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INTRODUCTION

FDI also provides the opportunities for the employment as the economic growth of the industries tends to enhance. FDI is also helpful in increasing the GDP level. As a result of FDI, the flow of physical capital tends to increase.

Due to increase in the physical capital flow, the rate of growth of economy also tends to enhance. FDI is that kind of investment where the domestic industries need not to bother about the financial aid as most of the financial needs are covered with the help of investment done by foreign institutes.

There are many sectors in India where the growth rate is not too much as there is so much financial debt on the industries. In these kinds of cases, if the industries have the enough potential to grow further then foreign direct investment proves to be beneficial for these industries as the growth bar tends to enhance effectively.

Recently, Indian government has the proportion of FDI in different government sectors like Defense, Agriculture and Railway etc. The primary motive for this increase in the FDI level is the economic growth in these sectors.

In India, there are also a number of private and public banks where foreign direct investment is imposed. In most of the cases, it is observed that FDI has certainly proved to be effective step in enhancing the economic growth of these banks.

Hence, from banking to defense sector and defense sector to the agricultural sector and railway sector, this trend of foreign direct investment has proven to be effective in raising the bar of growth of these industries.

The developing countries are now shifting their priorities from import substitution towards structural adjustments via free market economies and increasing emphasis on FDI. The latter is now accepted as panacea for all types of scarcities of financial capital, technological know-how, efficient managerial techniques, organizational skill and access to market abroad. As against portfolio investment, FDI is a source of creation of tangible and intangible assets, employment and wealth in the host economy. It may provide rents, potential spillovers and externalities that are highly beneficial to the host country's economic growth. Foreign Direct Investment (FDI) has increasingly been viewed as a catalyst to economic growth, particularly in developing countries.

FDI inflows can be a tool for bringing knowledge, managerial skills and capability, product design, quality characteristics, brand names, channels for international marketing of products, etc. and consequent integration into global production chains, which are the foundation of a successful exports strategy.

IMPLICATIONS OF FDI IN INDIA

FDI could benefit both the domestic industry as well as the consumer, by providing opportunities for technological transfer and upgradation, access to global managerial skills and practices, optimal utilization of human capabilities and natural resources, making industry internationally competitive, opening up export markets, providing backward and forward linkages and access to international quality goods and services and augmenting employment opportunities. For all these reasons, FDI is regarded as an important vehicle for economic development particularly for developing economies. FDI flows are usually preferred over other forms of external finance because they are non-debt creating, non-volatile and their returns depend on the performance of the projects financed by the investors. In a world of increased competition and rapid technological change, their complimentary and catalytic role can be very valuable.

However, these benefits do not come alone. The adverse effect of FDI inflows to the host country (i.e., developing one) should not be overlooked. Firstly, larger foreign firms may take dominant market shares, thereby reducing competition. Because of their economic power, they can establish monopoly position in the host country market and exploit resources more cheaply. Secondly, large foreign firms lead to negative effects on local firms and employments because they can crowd out small domestic firms. Thirdly, export and import activities of foreign-owned firms may lead to balance of payment

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volatility. Fourthly, when profits and capital of MNEs are repatriated, the value of the home currency may decline. But such costs can be corrected through appropriate host country policy measures.

According to the OECD report on foreign direct investment for development, the benefits of FDI do not occur automatically. The policies in both host countries and home countries matter. Only enterprises that operate in a generally sound national and international environment can bring the full benefits of FDI on the host economy.

As far as sectoral distribution of FDI is concerned, Electrical equipments (including computer software and electronics), Transportation industries, Services sector, Telecommunications, Fuels (Power and refineries), Chemicals (other than fertilizers), Food processing industries, Drugs and pharmaceuticals, Cement & gypsum products and Metallurgical industries were the dominant sectors inviting 16.50, 10.34, 9.64, 9.58, 8.41, 5.86, 3.67, 3.18, 2.54 and 2.10 per cent of the total FDI respectively.

More recent studies have focused on such factors as technological status, brand name, openness of the economy, macro trade policies of the government and intellectual property protection. Some of these variables are country specific rather than pertaining to a specific region or a State within a country. Keeping the above in mind the present study will focus on the trends and behaviour of FDI in India since 1991.

FDI are investments made by residents of one economy with the objective of establishing a lasting interest in a company located in another economy (host economy). With `lasting interest' we mean both the existence of a long-term relationship and a degree of ownership of the foreign firm. In statistics, ownership of at least 10 percent of the ordinary shares in US, India etc. and 25 per cent in Britain has been the criterion for the existence of a direct investment relationship. Ownership of less than 10 percent is considered as a portfolio investment. The presence of foreign investors means that firms controlled by foreigners produce part of domestic output. Foreign direct investment has grown at rates far beyond those of international trade since the late 1980s. Especially in the second half of the 1990s, firms were exceptionally active in cross border Mergers and Acquisitions (M&A). The outstanding global stock of FDI more than doubled in ten years time from 8.3 percent of world output in 1990 to 17.5 percent in 2000. It is conceivable that the larger presence of FDI is partly responsible for the observed increase in cross-country business.

DISCUSSION

According to the IMF's Balance of Payments Manual 5th Edition , along with OECD's Benchmark Definition of Foreign Direct Investment 3rd Edition (OECD 1999), FDI is defined as: '[...] the objective of obtaining a lasting interest by a resident entity in one economy ("direct investor") in an entity resident in an economy other than that of the investor ("direct investment enterprise")'.

FDI can be categorized into three components: equity capital, reinvested earnings and intra-company loans. *Equity capital* comprises of the shares of companies in countries foreign to that of the investor. *Reinvested earnings* include the earnings not distributed to shareholders but reinvested into the company. *Intra company loans* relate to financial transactions between a parent company and its affiliates.

FDI is an investment made to acquire a lasting management interest (normally 10% of voting stock) in a business enterprise operating in a country other than that of the investor defined according to residency.

The arguments for the positive impacts of FDI centre around three prevalent benefits that are important to a developing country, inflow of physical capital, technology spillovers, and employment. Inflow of physical capital in the form of FDI could also increase the rate of economic growth particularly for developing one where capital is scare. The leakage of technology spillover from MNEs enables domestic firms to improve their productivity and that allows the host country to enhance its long-term economic development. The growth enhancing ability of FDI also depends on the chosen mode of FDI. Greenfield FDI can result in an increase in the host country's stock of capital whereas the Brownfield FDI (M&A) can only result in positive externalities of technological spillover.

The Foreign Direct Investment has been one of the economic aspects where 'economics' and 'politics' remained closely interwoven. The two major reasons for attracting foreign direct investment are that it adds to the total investible resources on one hand and acts as a vehicle for transferring various advanced technological and managerial skills on the other hand. It must be noted that attraction of FDI is significant in the economies of the developing countries. In addition to this FDI can also contribute toward debt servicing repayments, stimulate export markets and produce foreign exchange revenue. Further FDI may stimulate product diversification through investments in new business, reducing market dependence on a limited number of products.

CONCLUSION

Developing economies search for FDI as a source of economic growth and development, modernization and employment generation. FDI can also do much for productivity- by providing access to new technologies, management expertise and export markets. And found that, why FDI need investment climate? If India wants attract FDI, it has considerably cut its bureaucratic structure and makes more efficient the system of licenses and clearness at a single window. Further, India has to develop its infrastructure including ports, airports, roadways, and rail network and guarantee a solid supply of power to foreign investors.

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