International Journal of Innovative Research in Management Studies (IJIRMS)
Volume 3, Issue 1, February 2018. pp.47-51.

IMPACT OF FOREIGN DIRECT INVESTMENT ON INDIAN ECONOMY

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Abstract—*FDI (Foreign Direct Investment) in India bound a vital role in the economic affair and development of India. FDI has innumerous sectors which will achieve intensification in economy through formation of jobs. With the commencement of globalization, developing countries particularly in Asia, have been witnessing a immense rush of FDI inflows during the past two decades. Even though India has been a latecomer to the FDI compared to other Asian countries, its sustainable market potentiality and the liberalized policy control has sustained its attraction as a favorable destination for foreign investors. It may also be affected due to the governmental trade barriers and policies for the foreign investments. It is considered as an important tool for economic growth in the developing countries, it affects by stimulating the domestic investment, increasing the formation of human capital and by smoothening the technology transfer in the host countries. FDI always contributes a positive growth towards the economic development of one country due to the investment made by another country or country's personnel's. If the investment is viewed with the motive of long terms investment in the social-economic development then it is rightly said that the investment contributes in a positive trend towards global economy, if it is viewed in short term investment for the purpose of making profit then it may be less significant than that of long term which might lead to negative effect. In past few decades, foreign direct investment has been an increasing trend in worldwide and has been acting as a useful instrument to enhance economic growth in developing countries. Many developing countries like India fear that by opening up markets to global competition and inviting foreign investment without restriction might lose control over strategic industries and influences on national security, social stability and economic development. This research paper aims to examine the impact of FDI on the Indian economy and also its major features, types and pros and cons to get clear vision of FDI in Indian economy.*

Keywords—*Developing Countries, Economic Growth, Foreign Direct Investment, Globalization, Indian Economy.*

INTRODUCTION

Foreign investment plays a vital role in development of Indian economy. Need of FDI depends on saving and investment rate in a country. Foreign Direct investment acts as a bridge to fulfil the gap between investment and saving. In the process of economic development foreign capital helps to cover the domestic saving constraint and provide access to the superior technology that promotes efficiency of the existing production capacity and generate new production opportunity. Many countries provide many benefits to attract foreign direct investment. During the past 15 years, the importance of FDI in the world economy has been in increasing trend. This increase in FDI has been specifically pronounced in developing countries, which largely reflects in the integration of large emerging economies, the so-called BRICs (Brazil, Russia, India and China), into the world economy. The increase of FDI into developing countries has been spectacular.

FDI or Foreign Direct Investment, is Fund flow between the countries in the form of Inflow or outflow by which one can able to gain some benefit from their investment, whereas another can exploit the opportunity to enhance the productivity and find out better position through performance. Flow of Foreign Direct Investment has shown a significant growth in recent times. Higher flow of Foreign Direct Investment over the world would reflect a better economic environment in the presence of economic reforms and investment-oriented policies. The potential advantages of the FDI on the host economy, facilitates the ease of access to new technologies. Higher inflows of FDI to a country, generates employment in the nation.

Over recent years most of the countries in the world have made their business environment investment friendly for absorbing global opportunities by attracting more FDI funds to the country. There are two types of FDI i.e inward foreign direct investment and outward foreign direct investment, which results in a net FDI inflow (positive or negative) and stock of foreign direct investment, which is the cumulative number for a given period. Direct investment excludes investment through purchase of shares. FDI is one example of international factor movements. Indian Economy has shown impressive growth over the liberalization period. With the help of economic indicators, growth and development of the country have been measured. In recent times Indian markets seek the attention of various foreign investors also government of India have liberal attitude towards FDI.

REVIEW OF LITERATURE

Srivastava, S. (2003) has examined the long-run relationship of FDI with the Gross Output, Export and Labour productivity in the Indian economy with the help of annul data. The researcher concludes that, in the eve of India's plan for further opening up of the economy, it is advisable to open up the export-oriented sectors so that the higher growth of economy is achieved.

Dua, P. and A. I. Rasid (1998) examined the nexus between FDI and economic growth in recent literatures. The researcher concludes that liberalizing policy constraints, modest corporate tax and improving governance and transparency could help to substantially improve FDI flows.

Chakraborty, C. and P. Basu (2002) has stated that, it is recommended that outward oriented strategies and polices of attracting FDI pursued by developing countries to achieve higher rates of economic growth.

Alfaro L. (2003) indicated the development of domestic financial system facilitated FDI technology spillovers in order to enhance the economic growth of the country

Balasubramanyam V.N, Sapsford David (2007) suggested that India's requirement of FDI may be substantially lower than that of china because the structure and composition of their manufacturing sector consists of a substantial proportion of science based and capital-intensive industries.

FDI AND ECONOMIC GROWTH IN INDIA

The Indian economy has reached in the orbit of high rate of economic growth. The decade of 80's emerged as a beginning of the high rate of economic growth or at least a dramatic departure from the past growth performance. This trend continues in the nineties and further growth stimulus has occurred in the early 21st century. India is the third-largest economy in the world so it is preferred destination for FDI. Industrial policy in India has reduced the restrictions regarding licensing requirements, expansions and facilitated easy access to foreign technology and FDI. The future of indian economy is brighter because of its huge human resources, availability of large number of competened professionals, vast market for every product, increasing of consumerism, interest of foreign entrepreneurs in India.

Booming FDI in India is greatly believed to promote economic growth. It turns out that growth of FDI differs across sectors. FDI in the service sectors appears to have promoted growth in the manufacturing sector through cross-sector spillovers. Today India provides highest return on FDI than any other country in the world.

FEATURES OF FDI

- **Reduced Cost of Production:** FDI also benefits by reducing the cost of production. This situation prevails when the rules are less restrictive.
- **Higher Returns:** FDI is largly preferable due to higher return than any investment in the home country.
- **Economy Growth:** FDI helps developing countries in their economic development. It will benefit the country which accepts FDI, through increased job opportunities, better infrastructure and high standards of living.
- **Rapid Supply of Money:** FDI is major source of income for a country. The country with limited amount of capital can receive funds beyond national borders from rich country.

TYPES OF FOREIGN DIRECT INVESTMENTS

DIRECTION

Inward FDI

The FDI invested by other countries in our country is called inward FDI. It includes interest loans, tax breaks, grants, subsidies and removal of restrictions and limitations.

Outward FDI

The investment made by our country in other country is rightly said to be outward FDI. This form of FDI is subject to tax incentives as well as disincentives of various forms. Risk coverage provided to domestic industries and subsidies granted to the local firms stand in the way of outward FDIs, which are also known as direct investments abroad.

TARGET

Greenfield Investment

Direct Investment in new expansion of exsisting facilities. Its objective is to create new production capacity and jobs. Profits earned from production does not go back into local economy but to MNC's economy.

Vertical FDI

Industry provides inputs or sells output from a firm's domestic production processes.

Horizontal FDI

Investment made in the same industry abroad as a firm operates from home.

MOTIVE

Resource Seeking

Motivated by investors interest in accessing and exploiting resources.

Market Seeking

Motivated by investor interest in serving domestic or regional markets.

Efficiency Seeking

FDI that enters into a country seeking to benefit from factors that enables it to compete in international markets.

IMPACT OF FOREIGN DIRECT INVESTMENT

FDI provides capital which is usually missing in the target country-Long term capital is suitable for economic development. Attracting foreign direct investment has become an integral part of the economic development ideas for India. The major step towards the economic growth of the country is, FDI ensures a huge amount of domestic capital, production level, and employment opportunities in the developing countries. In incorporating a range of well-composed and effective policies will boost up the profit ratio from Foreign Direct Investment. A huge inflow of FDI in various industrial units in India has boosted the economic life of country.

Positive Impact of FDI:

Positive impacts of FDI on India economy have been listed below:

- Economic growth is one of the major sectors, which is hugely benefited from foreign direct investment. Foreign direct investment would allow India to secure foreign infrastructure into India, which would increase India's capital base rapidly.
- Trade- Foreign Direct Investments have shared a wide range of opportunities in both trading of goods and services in India in terms of import and export production. Superior quality products are manufactured by various industries in India due to large amount of FDI inflows in the country.
- FDI have made available a number of employment opportunities by setting up of industrial units in various corners of India.
- It also reduces spoilage and enables the delivery of affordable products to all customers.
- FDI bring new technologies that are usually not available in the target country. Various foreign firms are occupying a position in the Indian market through Joint Ventures and collaboration concerns.
- Foreign direct investments are in a way responsible for the development of backward areas.
- There are so many industries started by them in far reaching and backward areas have developed into industrial centre.
- The maximum amount of the profits gained by the foreign firms through these joint ventures is spent on the Indian market.
- Also foreign corporations give hand to change the economic structure of the target country with a good economic strategy government can attract companies from promising and innovative sectors.
- Foreign investments will lead to better infrastructure and strengthen rupee vale against global currencies.
- It also helps to strengthen the government budget. Involvement of FDI in India increases competition and breaks domestic monopolies. With these changes, India is now the most open economy in the world for FDI.

Negative Impact of FDI:

In spite of positive impacts mentioned above, FDI also has negative impacts as follows:

- The snag of foreign direct investment mostly occurs in case of operations related to distribution of the profits made on the investment and the personnel.
- One of the indirect drawbacks of foreign direct investment is that the economically backward section of the host country is always disturbed and faces issues when the flow of foreign direct investment is negatively affected.
- The various other stumbling in foreign direct investment can be captured where the host country has some kind of national secret i.e. which is kept confidential and could not be disclosed to the rest of the world.
- At some point of time, it has been understood that specific foreign policies are adopted, but which are not appreciated by the workers of the recipient country.
- Foreign direct investment, is been a pitfall for the people who plan their investment themselves.
- Foreign direct investment may involve huge travel and communications expenses.
- The differences of language and culture between the investor country and the host country would also create problems in case of foreign direct investment.
- One of the major downside of foreign direct investment is that, a company may also suffer the loss of its ownership to an overseas company. This has stated awareness to many companies to approach foreign direct investment with a certain amount of caution.
- The small businessmen and the cottage industry would face extinction from the market because they would not be in a position to compete with the big multinational giants with their immense resources and formidable marketing methods.
- Also, in order to capture the foreign market, the FDIs have gone to the extent of even corrupting the high officials or the political heads in various countries. These are the drawbacks of FDI.

CURRENT CHALLENGES AND IMPROVEMENT

India is definitely a remunerative place for FDI, but there is certainly some provocation and areas for improvement are still present. Until, these areas are sharpened to perfection, India will only stay in the process of becoming to number one place for FDI. India is focusing on maximizing political and social stability along with a regulatory environment. In spite of the obvious advantages of FDIs, there are quite challenges faced in India. India is definitely developing in a much faster pace now than before but in spite of that it can be identified that developments have taken place unevenly. To get the complete picture of growth, it is essential to make sure that the rural section has more or less the same amount of development as the urbanized ones. There must exist a common ground between the Parliament and the foreign countries which are investing in India. India must also focus on areas of poverty reduction, trade liberalization, and banking and insurance liberalization. This would increase the reforms in the FDI in the country.

CONCLUSION

It can be observed from the above article that FDI has helped to raise the output, productivity and export in India. India’s Foreign Direct Investment (FDI) policy has been gradually liberalized to make the market more investor friendly. The positive effects of inward FDI for workers in host economies suggest that FDI-friendly policies could be a useful component of an integrated policy framework for development. When designing policies to promote FDI, policy-makers should take into account that these may not only affect the volume of inward FDI, but also its composition and, as a result, its corresponding benefits. The country is consistently ranked among the top three global investment destinations by all international bodies, including the World Bank, according to a United Nations (UN) report. For Indian economy which has tremendous potential and so FDI had a positive impact. FDI inflow supplements domestic capital, as well as technology and skills of existing companies. It also helps to establish new companies. Al these contribute to economic growth of the Indian Economy. Therefore, in the eve of India's plan for further opening up of the economy, it is advisable to open up the export-oriented sectors and a higher growth of the economy could be achieved through the growth of these sectors.

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