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FDI INFLOW AND GDP GROWTH OF INDIA

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Abstract:-

The major objective of this paper is trying to examine how far the FDI inflow in India is being influenced the growth of Indian Economy. The paper has represented the importance of the FDI inflow and its significance. The relevant and appropriate review of literatures also incorporated in this paper. Some of the important factors which affect the FDI inflow also discussed. Finally, the FDI inflow into India and GDP growth has been compared and tested by Correlation techniques.

Keywords: FDI inflow in India, GDP growth, Factors determining the FDI.,

1. INTRODUCTION

Foreign Direct Investment (FDI) plays a pivotal role in the Economic development of the nation. In other words FDI plays a vital role in the growth of underdeveloped and developing countries. FDI is an investment made by a foreign individual or a company in the productive capacity of another country. It can be considered as the movement of capital across national frontiers in a manner that allows the investor to have a control over the investment. Firms that provide FDI are referred to as MNCs. The investors can invest in existing industries/business or can promote new industries. There can be two types of FDI- inward and outward. The cumulative of two, results in net FDI inflow. FDI is freely allowed in all the sectors except a few sectors, though in certain sectors FDI is not allowed beyond a ceiling. FDI act as a long term source of capital as well as a source of advanced and developed technologies. The investors also bring along best global practices of management. As large amount of capital comes in through these investments more and more industries are set up. This helps to increase more potential growth in employment market and also helps in promoting international trade. This investment is a non-debt, non-volatile investment and returns received on these are generally spent on the host country itself thus helping in the development of the country. Some of the sectors that attract high FDI inflows in India are the hotel and tourism industry, insurance sector, telecommunication, real estate, retail, power, drugs, financial services, infrastructure and pollution control etc. India is trying to attract some of the key sectors like Railways and Defence.

2. OBJECTIVES

- To examine the FDI inflow in to India.
- To analyse the GDP at factor absolute cost.

To compare both FDI inflow and GDP annual growth.

- To correlate the FDI and GDP in absolute value.

3. REVIEW OF LITERATURE

Bhattacharyya Jita, Bhattacharyya Mousumi (2012) examined the impact of Foreign Direct Investment and Merchandise and Services Trade of the Economic growth in India: an Empirical study. The study revealed that there was a long Term relationship between FDI, merchandise, service trade and economic growth of India. Singh Y., Bhatnagar A.(2011), "FDI in India and China; A comparative analysis. He found that both enjoys healthy rates of economic growth but FDI inflow in china is Higher than India. A garwal G., Khan M. A.(2011) examined the impact of FDI on GDP: A Comparative Study of China and India. They found that 1% increase in FDI would result in 0.07% increase in GDPofChinaand0.02%increaseinGDPofIndia. Saini A., Law S. H., Ahmad A.H. (2010), "FDIand Economic growth: New evidence on the role of financial markets" It was proved that the positiveimpactofFDIon growth "kicks in" only after financial market development exceeds a threshold level.

Chee Y. L., Nair M. (2010) analysed the impact of FDI and Financial Sector Development on Economic Growth: Empirical Evidence from Asia and Oceania"The empirical analysis showed that financial sector development enhances the contribution of FDI on economic growth in the region.KumarG.L.,KarthikaS.(2010) analysed the Sectorial Performance Through InflowsofForeign Direct Investment (FDI). The study revealed that Foreign Direct Investment has a major role to play in the economic developmentofthehost country. Singh, Shikha(2009), "Foreign Direct Investment (FDI) and GrowthofStatesofIndia"This study stated that foreign direct investment (FDI) policies play a major role in the economic growthofdeveloping countries around the world. Acharyya J. (2009) analysed the FDI, growth and the environment: evidence from India on Co2 emission during the last two decadesshown that long run positive, but marginal, impact of FDI inflow on GDP growth in Indiaduring 1980-2003. Syed Zia A. R., (2009), "The Impact of Foreign Direct Investment on Employment Opportunities: Panel Data Analysis: Empirical Evidence fromPakistan, India and China"It was found that there is along term relationship between FDI and employment opportunities.Keshava, Dr. S.R. Rathnamma (2008), The EffectofFDIonIndia and Chinese Economy: A Comparative Analysis:stated that India and China are the two emerging economic giantsofthe developing world, both situated in Asia with 37%ofworld population (Asian Development Outlook2005) and with more than 9% growth in their respective GDPoftheir economies (World Development Report 2006). Most of the empirical works on the FDI-economic growth relationship have the neoclassical models as their basis. Chowdhury and Mavrotas (2005) identified four main channels through which this relationship has been studied. On the contrary some theories predict that distortions due to FDI pre-existing trade, price, financial, and others will lead to inefficient resource allocation and slow growth (Brecher and Diaz- Alejandro, 1977; Brecher, 1983; Boyd and Smith, 1992). These ambiguous predictions about the growth effects of FDI suggest that FDI will only promote growth under certain policy conditions. However, cross-section macroeconomic studies using aggregate FDI flows generally suggest a positive role for FDI in generating economic growth especially in particular environments (De Gregorio, 1992). Following Borensztein et al. (1998), FDI has a positive growth-effect when the country has a highly educated workforce. They believe that the educated

workforce fosters the exploitation of FDI spillovers.

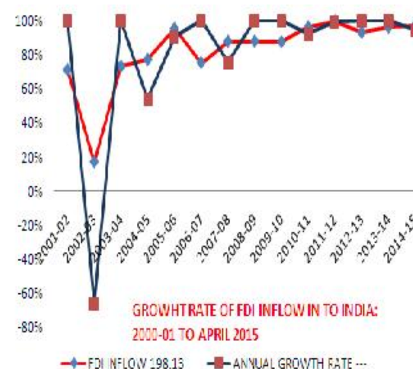
4. FDI INFLOW IN INDIA

India’s inward investment regime went through a series of changes since economic reforms were ushered in two decades back. The expectation of the policy makers was that an “investor friendly” regime will help India establish itself as a preferred destination of foreign investors. These expectations remained largely unfulfilled despite the consistent attempts to increase the attractiveness of India by further changes in policies that included opening up of individual sectors, lowering the hitherto existing caps on foreign holding and improving investment procedures. But after 2005–06, official statistics started reporting steep increases in FDI inflows. More recently, the Economic Survey 2008-09reiterated that:FDI is considered to be the most attractive type of capital flow for emerging economies as it is expected to bring latest technology and enhance production capabilitiesof the economy.(Emphasis added)And the National Manufacturing Competitiveness Council (NMCC) opined that:Foreign investments mean both foreign portfolio investments and foreign direct investments (FDI). FDI brings better technology and management, access to marketing networks and offers competition, the latter helping Indian companies improve, quite apart from being good for consumers. This efficiency contribution of FDI is much more important.

FDI INFLOW IN TO INDIA

YEAR	FDI INFLOW	ANNUAL GROWTH RATE
2000-01	198.13	---
2001-02	1036.12	422.88
2002-03	176.53	-859.59
2003-04	502.39	184.59
2004-05	201.32	-59.92
2005-06	182.93	-9.13
2006-07	457.28	149.97
2007-08	279.01	-38.98
2008-09	455.59	63.28
2009-10	1314.23	188.39
2010-11	858.03	-34.71
2011-12	826.16	-3.71
2012-13	2193.65	165.52
2013-14	25106.78	1044.52
2014-15	3164.72	-87.39

Source: DIPP



According to data on the Indian government’s DIPP website, the total FDI investments India received in January-June period of 2015 was $19.4 billion and in the whole of 2014, the country received $28.8 billion. In 2013, India received $22 billion FDI and $22.8 billion in 2012. According to the RBI data, India received $18.9 billion in the first half of 2015 and $26.4 in 2014 and $25.6 in 2013.Nevertheless, if one believes that there is merit in the FT numbers, this is big good news for India. But, if indeed India has emerged as the top FDI destination, in terms of investments in green field projects (measured by estimated capital expenditure), a major reason for that is the ongoing slowdown that has gripped rest of the world, primarily China. Remember, in the whole of last year (2014), China received FDIs worth $75 billion, while US received $51 billion. On the positive side, it would mean that the world is finding India as an important alternative, when others aren’t doing well, thanks to the strong economic fundamentals of the country and its huge untapped potential. This is indeed good news. The numbers are certainly a booster dose to the Narendra Modi-government, which is facing investor-pessimism.Notably, according to the FT report, this comes at a time when FDI

into emerging markets is showing a declining trend "with 97 of 154 countries typically classed as emerging markets experiencing declines in capital expenditure on greenfield investment projects in the first six months of this year compared with the same time period last year". Also, this comes close on the heels of a world economic forum report showing that India moved 16 positions up in the global competitiveness index to the 55th position on account of improvement in the country's macroeconomic environment and a 'slight' improvement in the infrastructure sector.If indeed the country has caught global investors' attention, the next big question is can the country sustain the performance seen in the first half, going ahead also, especially when global economy comes out of the woods? It's possible if the Modi government manages to use the current phase to set the economy on the high growth path and address the basic structural issues.These include sorting out the problems in taxation, repairing the critically damaged banking sector and ensuring ease of doing business by facilitating enabling factors (land, water, electricity, necessary clearances etc) to begin a business in India. While global slowdown is a blessing in disguise for India, to cash in on the opportunity, the country needs to fast track its reform agenda, besides improving the infrastructure sector. The RBI made a big move by affecting more than 50 basis points (bps) rate cut, which will eventually help bring down the cost of money in the financial system, both in the bank lending market and in the money markets. Already, the country's largest lender, State Bank of India, has taken the first move by announcing a 40 bps cut in its minimum lending rates, taking its base rate to 9.3 per cent now.RBI governor Raghuram Rajan's growth supportive move needs to be reciprocated by the government. Rajan had cautioned that the government too needs to do its part. "...Monetary policy has to be accommodative to the extent possible, given its inflation goals, while recognizing that continuing policy implementation, structural reforms and corporate actions leading to higher productivity will be the primary impetus for sustainable growth," Rajan said.India is certainly catching the attention of global investors, especially in the backdrop of a severe (and likely to be prolonged) global slowdown phase. If India has already managed to attract foreign investments, it is good news for the country, which needs at least $ 1 trillion investments to develop its roads, railways, ports and airports under the current five-year plan.

5. FDI INFLOW AND ECONOMIC GROWTH

A major component of capital flow for emerging developing economies is Foreign Direct Investment (FDI). There is however an argument on its contribution towards economic growth. As noted by Musila and Sigué (2006) most researchers agree that the benefits of FDI outweigh its cost to the particular economies. Carkovic and Levine (2002) find that FDI does not induce economic growth independently. The contribution of FDI to growth is affected by microeconomic conditions of the country as well as the host country's specific competitive advantage and its business environment. There exists scores of studies on the relationship between FDI inflows and economic growth. A plethora of studies also exist on the direction of causality between FDI and economic growth. Others have investigated it as nexus because of criticisms of a uni-directional causal relationship. As noted by Asafu-Adjaye (2005), the distrust of foreign direct investment (FDI) in the 1960s and early 1970s waned very fast and developing country governments have now come to embrace it recently. He noted that the growing interest in FDI is not only a result of globalization but also a consequence of the steady decline in official development assistance. A major source of capital for developing countries is FDI.

Economic theory postulates that, international capital inflows, inter alia, promote efficient allocation of resources, which in turn enhances economic growth. It may therefore be regarded as a catalyst for technology transfer from the developed to developing countries. Trying to explain economic growthis one of the fundamental questions in economics and has generated a large body of research. While the failure of the Solow model (Solow, 1956) to explain the large differences in income levels between countries has been interpreted as a result of differences in technology it was endogenous growth theory as presented in Romer (1986 and 1990) and Lucas (1988) that began toanalyse the relationship between technology and growth in detail. The importance of technology for economic growth provides an important link between FDI inflows and host country economic growth. It is theoretically straightforward to argue that inflows of FDI has a potential for increasing the rate of economic growth in the host country. Inflows of physical capital resulting from FDI could also increase the rate of economic growth but it is argued in this paper that the most important effect comes from spillovers of technology. MNE operations in the host country can result in technology spillovers from FDI whereby domestic firms adopt superior MNE technology which enables them to improve their productivity. Technology spillovers thereby generate a positive externality that should allow the host country to enhance its long-run growth rate.

Foreign Direct Investment is the important tool of globalization. FDI is the process whereby residents of one country (the source country) acquire ownership of assets for controlling the production, distribution and other activities of a firm in another country (host country). Foreign direct investment plays an important role of bridging the gap between the available resources or funds and the required resources or funds. In 2007 FDI inflow was 20 billion ,it increases up to 43.4 billion in 2008. Then it reduces to 35.6 billion in 2009 and in 2010 it reduces to 27.4 billion. In 2011 it again increases up to 36.5 billion. With the tripling of the FDI flows to EMEs during the pre-crisis period of the 2000s, India also received large FDI inflows in line with its robust domestic economic performance. The attractiveness of India as a preferred investment destination could be ascertained from the large increase in FDI inflows to India, which rose from around US$ 6 billion in 2001-02 to almost US$ 38 billion in 2008-09. The significant increase in FDI inflows to India reflected the impact of liberalization of the economy since the early 1990s as well as gradual opening up of the capital account. As part of the capital account liberalization, FDI was gradually allowed in almost all sectors, except a few on grounds of strategic importance, subject to compliance of sector specific rules and regulations. The large and stable FDI flows also increasingly financed the current account deficit over the period. During the recent global crisis, when there was a significant deceleration in global FDI flows during 2009-10, the decline in FDI flows to India was relatively moderate reflecting robust equity flows on the back of strong rebound in domestic growth ahead of global recovery and steady reinvested earnings (with a share of almost 25 per cent) reflecting better profitability of foreign companies in India. However, when there had been some recovery in global FDI flows, especially driven by flows to Asian EMEs, during 2010-11, gross FDI equity inflows to India witnessed significant moderation. Gross equity FDI flows to India moderated to US$ 20.3 billion during 2010-11 from US$ 27.1 billion in the preceding year.

INDIA'S GDP AT FACTOR COST

YEAR	GDP Factor Cost (Rs.in Crores)	ANNUAL GROWTH RATE
2000-01	1211747	---
2001-02	1258231	3.83
2002-03	1320313	4.93
2003-04	1426701	8.05
2004-05	1529408	7.19
2005-06	2595339	69.69
2006-07	2848157	9.74
2007-08	3122862	9.64
2008-09	3339375	6.93
2009-10	4464081	33.68
2010-11	4877800	9.26
2011-12	5202500	6.65
2012-13	6520125	19.56
2013-14	8083722	23.95
2014-15	12507000	54.71

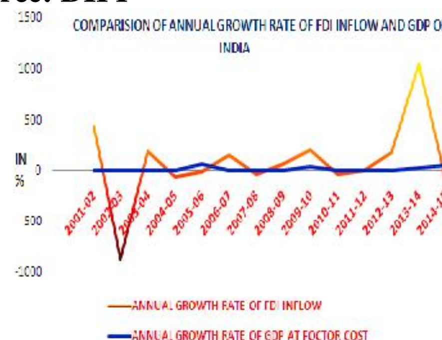
Annual Growth Rate of India's GDP at factor cost was really amazing with high fluctuation. It was recorded just 3.83 percent during 2001-02. It was reached 69.69 percent at factor cost in absolute valueduring 2005-06 there was highest boost in the economy.Indian economy, growing at a pace next only to China, expanded at a faster rate of 9.0 per cent during 2005-06 largely on the back of a higher output in farm sector than previously estimated. The government on Wednesday revised upward its growth estimates for the last financial year to 9.0 per cent as against 8.4 per cent earlier, boosting hopes of the economy touching an overall 8.0 per cent in the 10th five-year plan.According to official figures, the growth rate of 9 per cent in GDP during 2005-06 was achieved due to high growth in agriculture, forestry and fishing, manufacturing, insurance, construction, financing, real estate and business services and transport.Manufacturing is shown a shade better at 9.1 per cent as against the previous figure of 9 per cent. With the revision in the figures by the Central Statistical Organisation, the GDP growth shows a significant improvement for the previous financial year over 2004-05.If the trend of the first half of the current financial year continues for the rest of 2006-07, it would be for the second year in a row that the country's GDP would grow by 9 per cent with the distinction of being the second fastest growing economy in the world, after China

COMPARISION OF ANNUAL GROWTH RATE OF FDI INFLOW AND GDP OF INDIA

YEAR	ANNUAL GROWTH RATE OF FDI INFLOW	ANNUAL GROWTH RATE OF GDP AT FOCTOR COST
2001-02	422.88	3.83
2002-03	-859.59	4.93
2003-04	184.59	8.05
2004-05	-59.92	7.19
2005-06	-9.13	69.69
2006-07	149.97	9.74
2007-08	-38.98	9.64
2008-09	63.28	6.93
2009-10	188.39	33.68
2010-11	-34.71	9.26
2011-12	-3.71	6.65
2012-13	165.52	19.56
2013-14	1044.52	23.95
2014-15	-87.39	54.71

Source: RBI Bulletin.

Source: DIPP



Correlation Co-efficient

VARIABLES	FDI INFLOW	GDP
FDI INFLOW	**1**	**.66**
GDP	**.66**	**1**

Source: Estimated.

The Gross Domestic Product (GDP) in India was worth 2066.90 billion US dollars in 2014. The GDP value of India represents 3.33 percent of the world economy. GDP in India averaged 550.27 USD Billion from 1970 until 2014, reaching an all time high of 2066.90 USD Billion in 2014 and a record low of 63.50 USD Billion in 1970. GDP in India is reported by the World Bank Group. The correlation co-efficient indicates that both GDP and FDI inflow has correlated .66 unit which indicates that FDI inflow has positively influenced the Growth of GDP.

CONCLUSION

According to data on the Indian government's DIPP website, the total FDI investments India received in January-June period of 2015 was $19.4 billion and in the whole of 2014, the country received $28.8 billion. In 2013, India received $22 billion FDI and $22.8 billion in 2012. According to the RBI data, India received $18.9 billion in the first half of 2015 and $26.4 in 2014 and $25.6 in 2013.Nevertheless, if one believes that there is merit in the FT numbers, this is big good news for India. But, if indeed India has emerged as the top FDI destination, in terms of investments in green field projects (measured by estimated capital expenditure), a major reason for that is the ongoing slowdown that has gripped rest of the world, primarily China. Remember, in the whole of last year (2014), China received FDIs worth $75 billion, while US received $51 billion.The correlation co-efficient indicates that both GDP and FDI inflow has correlated .66 unit which indicates that FDI inflow has positively influenced the Growth of GDP. The large and stable FDI flows also increasingly financed the current account deficit over the period. During the recent global crisis, when there was a significant deceleration in global FDI flows during 2009-10, the decline in FDI flows to India was relatively moderate reflecting robust equity flows on the back of strong rebound in domestic growth ahead of global recovery and steady reinvested earnings (with a share of almost 25 per cent) reflecting better profitability of foreign companies in India. However, when there had been some recovery in global FDI flows, especially driven by flows to Asian EMEs, during 2010-11, gross FDI equity inflows to India witnessed significant moderation. Gross equity FDI flows to India moderated to US$ 20.3 billion during 2010-11 from US$ 27.1 billion in the preceding year.

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