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FDI TRENDS IN INDIA: A MULTI-DIMENSIONAL ANALYSIS

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ABSTRACT
The saga of FDI trends in India, over the past two decades, signifies the sustained gentrification of foreign investment confidence. Though subject to erratic downfall, it did not impede the enthusiasm of external investors in India. The database shows that FDI has been growing sizably in the fertile soil of the Indian economy, which was reconditioned by the eventful economic restructuring initiatives. This paper analyses the growth trends of inward FDI in India from 1990-91 to 2009-10 on a multi-dimensional perspectives. Along with the annual trend, decadal and five year growth trend has also been analyzed to understand the periodical phenomena. The paper reviews the main policy framework on FDI, suggests further policy guidelines for the future as well to enable the country to be an enduring liberal and seemingly attractive investor-friendly investment climate.

KEY WORDS
FDI, Indian Economy, New Economic Policy, Globalization, FDI policy.

INTRODUCTION
Disillusioned by the setbacks to heavily state-protected economies in general, and the disintegration of the USSR in particular, gave a room for India to have an objective re-look to the stifling regulative regime and the feeble knots of bureaucracy. Coincidently, the fascinating waves of LPG (liberalization, privatization and globalization) started enticing the national economies across the world. India was not hesitant to follow suit. Despite the conditionality for enabling financial accommodation for an economy, which was near the brink of collapse, India was also lured into the euphoria of openness. As a result, the business atmosphere in India was transferred from license permit raj to laissez-faire, which is superseded by single window clearance system for many privileged ventures. The Nehruvian vision of isolationism and bureaucratic control (Cappelli et. al., 2010) helped the country barely to achieve almost consistently a meager Hindu rate of growth, as it was referred in the economic literature, which was not at all sufficient enough even to cover up the constantly rising population. International credibility of the country was abjectly low. It was evidenced from the low level of foreign exchange reserve, which was not enough to meet two weeks export bill in 1991. In this backdrop, India initiated its economic restructuring with a clear road map. After three years of bottleneck, the macro economic reform programme started showing promising signals. The approach towards foreign investments, backed by considerable strides in enabling business friendliness, has been progressively favourable. Throughout the restructuring process the business and economic policy regimes were enviably growth-oriented and stabilizing. It has been corroborated from the high annual GDP growth rate and the perceptible capability of the country to withstand the East Asian crisis in the late 1990s and the recent financial turmoil that shook the world economies, shattering the business confidence across the world.

Inward FDI has a major role to play in shaping the structure of host economies. India is a perennial beneficiary of this bounty. The government initiated a dramatic liberalization of its regulative regime governing inward FDI in 1991 in tandem with the implementation of the new economy policy. The reforms initiated included the abolition of the mandatory industrial licensing system, the opening up of areas in which foreign participation was previously excluded and the establishment of the Foreign Investment Promotion Board. The recent UNCTAD (2009) survey finding puts India as the most preferred destination for foreign investors, second only to china.

PURPOSE OF THE STUDY
The overall objective of the study is to examine the chronological trends in India's FDI inflows from 1990-91 to 2009-10 on a multi-dimensional perspective.

RESEARCH METHODOLOGY
The present study followed an analytical approach to chronological quantitative data. The database on FDI published by the Directorate of Industrial Policy and Promotion (DIPP), India and the Centre for Monitoring of Indian Economy (CIME) for the period between 1990 – '91 and 2009 – '10 was obtained for trend analysis. The DIPP database was procured from the official web page and that of CIME was from its monthly publications. The growth trend was analysed in four levels for the period under consideration. The annual growth trend was estimated as a first step of analysis. These annual trends were averaged on a five year, ten year and eventually on an overall level to unfold and decipher the multi-dimensional trends and implications. As a prelude to trend analysis, the policy implications were reviewed to understand the institutional framework of FDI policy.

GLOBAL TRENDS IN FDI
Global FDI inflow was estimated as $ 193 billion during the year 1990 (UNCTAD, 1991). The share of developed and developing countries was $163 billion and $30 billion respectively. During 1999, the FDI inflow of the world increased to $865 billion. Out of it the share of developing countries was $208 billion, showing an apparent increase in the stake of growing economies in the global inward FDI flows. The current global financial crisis has had a dampening effect on FDI (UNCTAD, 2009). World Investment Report (UNCTAD, 2009) discloses that the global trends in FDI inflows show a declining trend continuously during 2008 and the first quarter of 2009, immediately after an unprecedentedly record peak during 2007. The widespread significance of inward FDI is widely recognized as the off-shoot of rapid technological change, intensified competition and economic liberalization (UNCTAD, 2000). As global FDI flows are expected to jump from $1.2 trillion this year to $1.6 to $2.0 trillion in 2012, changing ecosystem of foreign investment in India could pay rich dividends as it is observed by World Investment Report 2009 (UNCTAD, 2009).

POLICY IMPLICATIONS
The economic crisis during 1990-91 triggered more comprehensive and sustainable reforms in India. These policies have provided ample opportunities to build strong foundations for planned economic development (Reddy, 2009). Dismantling barriers for ensuring free flow of capital was an essential component of the New Economy Policy initiatives 1991, which enabled removing the restriction on inward FDI in the country. As a start up initiative permission was granted to

foreign investment aimed at encouraging foreign trading companies to assist Indian exporters in export activities, by approving FDI equity participation up to 51% in high priority industries (GoI, 1992).

The foreign investment was further liberalized in 1993 by removing the conditionality of dividend balancing for non-consumer goods. Decisive policy decisions appeared during 1996 – 1997. The FDI limit was raised up to 74 per cent, under the automatic route by RBI in nine categories of industries in infrastructure sector. In 1997 the first ever guidelines for FDI for expeditious approval of foreign investment, in areas not covered under automatic approval, was announced. In 1999, in terms of procedures, automatic approval for foreign equity participation up to 100 per cent is permitted for electricity generation, transmission and distribution for foreign equity investment not exceeding Rs.1500 crore (excluding atomic reactor power plants). In 2000-2001 the time frame for consideration of FDI proposals was reduced from 6 weeks to 30 days for communicating Government decisions. In august 2001 the Planning Commission appointed a Steering Committee on FDI with a mandate of streamlining foreign investment. In a major breakthrough FDI up to 100 per cent is allowed under automatic approval for most sectors/activities, where the prior approval is not required. Foreign investment limit in the private sector banking was raised to 74 per cent under automatic approval. As a result of the comprehensive review of the FDI policy, wide-ranging policy changes were notified in 2006, extending automatic routes, increasing equity caps, removing restrictions, simplifying procedures and extending the horizon of FDI to vistas like single brand product retailing and agriculture (GoI, 2008a). In a major policy initiative, during 2008, the sectors, in which FDI was prohibited, were specified. These areas are retail trading (except single brand product retailing), atomic energy, lottery business, gambling and betting, business of *chit fund*, *nidhi* companies, trading in transferable development rights and activities/ sectors not opened to private sector investment (GOI, 2009).

The latest policy document on FDI was released on 31st March 2010, whereby this document now consolidated all existing regulations related to FDI contained in FEMA, the comprehensive policy document came into effect from April 1, 2010 and would be replaced every 6 months after incorporating the changes which have been effected during the period. This step will improve the transparency and boost confidence level of global investors' community. The present policy reveals that 100 per cent FDI is permitted under automatic route in most of the sectors while there are sectoral caps, in the case of banking (74%), Insurance (26%), Telecom (49%), Aviation (74%) and single brand retail (15%) etc. Certain sectors like atomic energy, lottery, gambling and betting, multi brand retail etc., are not yet permitted (GoI, 2009). Government's recent proposal to allow up to 49% FDI limit in defense and entry in multiple brands in retail have a serious discussion on different forums and revealing different versions of the stakeholders leads to examining multiple dimension of recent policy initiations. The Indian polity is also planning to initiate the full convertibility of rupee on a phased manner (current account convertibility was announced in 1994).

The institutional mechanism established for FDI growth in India has five major components. Firstly, the establishment of Foreign Investment Promotion Board (FIPB) for reviewing and recommending the FDI proposals, which do not come under the automatic route. approval holders in obtaining various approvals and resolving their operational difficulties. Secondly, the constitution of Foreign Investment Promotion Council (FIPC) to undertake vigorous investment promotion and marketing activities. Thirdly, Financial Investment Implementation Authority (FIIA) was constituted for assisting the FDI. Fourthly, The Foreign Exchange Management Act (FEMA) has been introduced as Enforcement Directorate, replacing the much punitive Foreign Exchange Regulation Act (FERA), with a broad aim of consolidating and amending the law relating to foreign exchange with objective of facilitating external trade and payments and for promoting the orderly development and maintenance of foreign exchange market in India. Lastly, constitution of Investment Commission (IC) for facilitating meetings and visits industrial groups and houses in India and large companies abroad in sectors where there was dire need for investment.

TRENDS IN FDI INFLOW

The pattern of FDI inflow to India, over the last twenty years, shows a rising trend, with 36.1 per cent growth rate on an average, with erratic oscillations. It is a clear indication of the international business confidence on India. A generally accorded prediction is that India would be the next super power (GOI, 2008b). Both policy and structural changes are being taken place in India that are conducive for building business confidence and, thereby, furthering international business partnership creating all-season investment enabling climate.

The saga of FDI inflow to India is worth analyzing. A cursory analysis of the chronological data during immediately preceding two decades discloses that FDI is growing at a rate of 36.1 percent on a twenty year over all average (refer table 1). Splitting the twenty year span into two decades, the FDI growth rate shows an almost consistent level to the overall percent, being 36.78 per cent during the first decade and 35.62 per cent during the second decade. The economic confidence of world economies was shattered by periodical business and economic turbulence. However, the business confidence of global investors on India continued to be positive, though subject to erratic disturbances, as evidenced by the statistics. Over the years three financial years (1992-93, 1994-94 and 2006-07) were remarkable with FDI growth rates crossing 100 percent over the immediate preceding years. Within two years of economic restructuring policy of India the FDI inflow recorded all time highest growth (202.31 per cent) during 1992-93. It can be inferred from the date that foreign investors were waiting at the door steps of India, as they rushed in when the economy started opening up.

TABLE 1: INDIA'S FDI GROWTH TREND (1990 – 91 TO 2009-10)

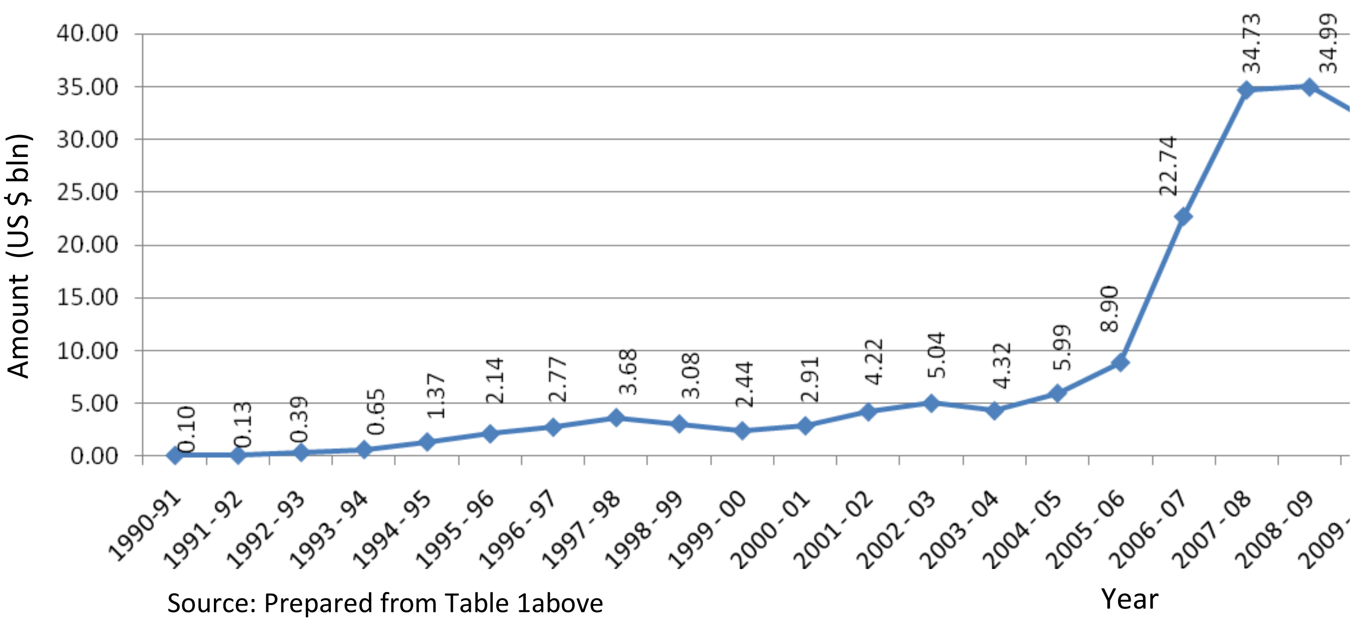
Year	FDI (US $ bln)	Growth rate (%)	Five year average (%)	Ten year average (%)	Overall average (%)
1990 - 91	0.10	0			
1991 - 92	0.13	30			
1992 - 93	0.39	202.31	88.25		
1993 - 94	0.65	66.41			
1994 - 95	1.37	110.09			
1995 - 96	2.14	55.82		36.78	
1996 - 97	2.77	29.38			
1997 - 98	3.68	32.92	16.19		
1998 - 99	3.08	-16.27			
1999 - 00	2.44	-20.89			
2000 - 01	2.91	19.23			36.1
2001 - 02	4.22	45.19			
2002 – 03*	5.04	19.28	21.61		
2003 – 04*	4.32	-14.18			
2004 – 05*	5.99	38.52			
2005 – 06*	8.90	48.67		35.62	
2006 – 07*	22.74	155.47			
2007 – 08*	34.73	52.72	49.63		
2008 – 09*	34.99	0.76			
2009 – 10*	31.68	-9.46			

Source : http://dipp.nic.in/fdi_statistics/india_yearwise.pdf

**Center for Monitoring of Indian Economy(CMIE), July 2010, P.7*

The inward FDI accumulated an ever time higher amount of $34.99 billion during 2008-09, followed by a down fall in the next year. This accomplishment is quite incredible when it is known that FDI inflow during 1990-91 was a paltry amount of $0.10 billion. To understand the periodical trends in FDI inflow, the twenty year time frame was divided into four quarters, each comprising of five years and finding five year average for each quarter. The highest rate of growth recorded during the first quarter (88.25 per cent). This quarter was notable due to a few of other factors also. Firstly, the highest annual growth rate recorded during this quarter (202.31 per cent in 1992-93). Secondly, not a single year registered negative growth. Thirdly, FDI growth rate crossed 100 percent limit in two alternate years. Lastly, the single quarter that registered constant rising trend (refer figure 4.a).

FIGURE 1: OVERALL GROWTH TRENDS OF FDI INFLOW (1990-91 TO 2009-10)



Source: Prepared from Table 1above

A close examination of the second quarter (1995-96 to 1999-00) unveils the following trends. Firstly, the positive growth trend continued (though subject to oscillation) during the initial three years. Secondly, the last two years of this quarter registered setbacks, the highest negative accumulated growth in the overall scenario. Contradictory to the global trend (refer UNCTAD, 2000), inward FDI to India experienced a continuous decline during this period. These setbacks were due to the unfavourable FDI policy by the new political party at power (however they overhauled their policy later). Those who are aware of the East-Asian currency crisis towards the close of last century can easily understand that the reason for this reverse gear was the repercussion of the collapse of Asian Tigers. Lastly, the five year trend is showing a perfect inverted 'U' hypothesis (refer figure 4b) and recorded the lowest quarterly average (16.19 per cent) in the reference period.

The third quarter was relatively better than the previous quarter, being the quarterly average 21.61 per cent. This quarter experienced a cyclical trend in FDI flow. The last quarter witnessed an optimistic growth patterns as the rate of growth (49.63 per cent) got back to higher plateau after low growth rates during previous two consecutive quarters. An appreciable growth in FDI inflow (155.47 per cent) was witnessed in during 2006-07 (immediately preceding the global financial turmoil). It has been followed by a continuous down fall and eventually set back in 2009-10. The FDI inflow touched its ever recorded highest level ($34.99 billion) in the Indian economic history in 2008-09, when the world economies were engulfed by global financial landslide and the global inward FDI encountered a negative growth trend (UNCTAD, 2009).

FIGURE 2: DECADAL GROWTH TRENDS OF FDI INFLOW (1990-91 TO 1999-00)

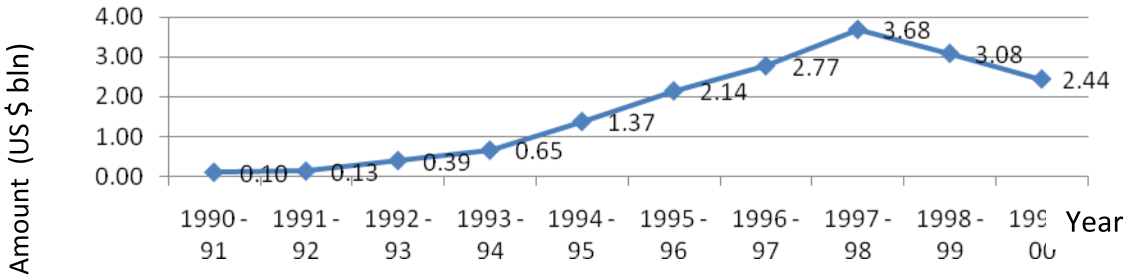


FIGURE 3: DECADAL GROWTH TRENDS OF FDI INFLOW (2000-01 TO 2009-10)

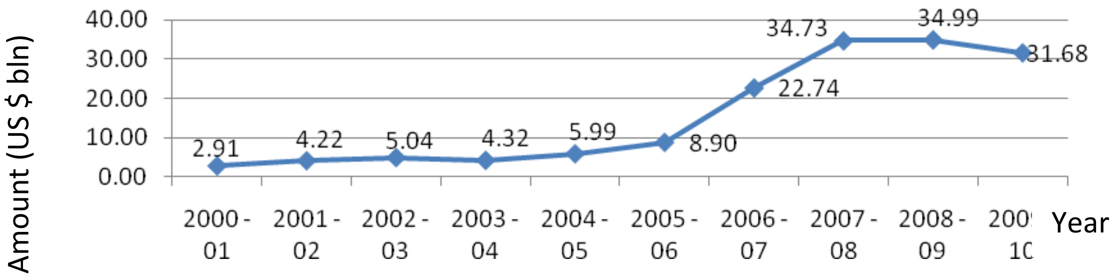


FIGURE 4A: FIVER YEAR GROWTH TRENDS (1990-91 TO 1994-95)

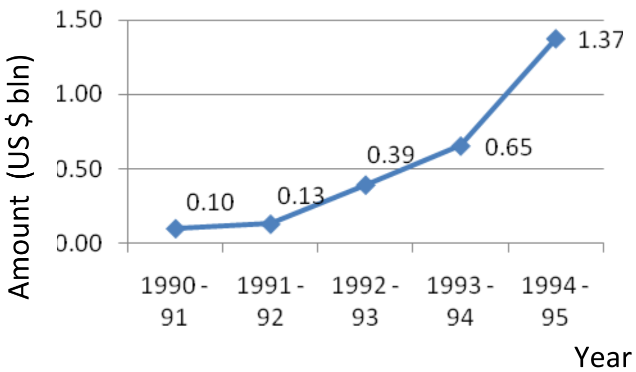


FIGURE 4B: FIVER YEAR GROWTH TRENDS (1995-96 TO 1999-00)

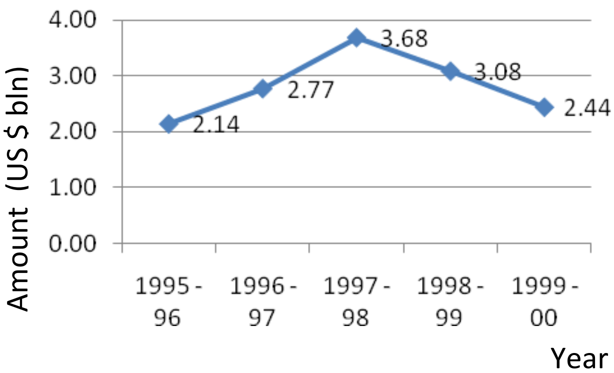


FIGURE 5A: FIVER YEAR GROWTH TRENDS (2000-01 TO 2004-05)

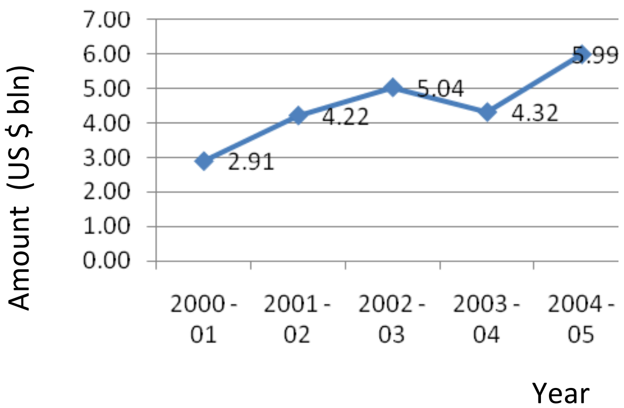
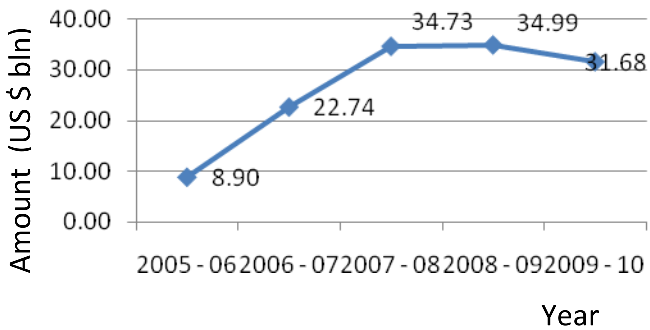


FIGURE 5B: FIVER YEAR GROWTH TRENDS (2005-06 TO 2009-10)



THE ROAD AHEAD

Efforts are on to reinforce the competitiveness of India as a first choice investment destination. The road ahead for India is not seemed to be smooth, when the world economies are contesting to woo foreign investors. We need shore up transparency and rationalize the rules and extend the cap limit to different sectors and allow new sectors in FDI list leads to tap good inflows to India, but no one can ignore that a liberal FDI regime is bound to act as a springboard for attracting foreign investors to India's near double digit growth story.

The Foreign Direct Investment Confidence index prepared by the global management consulting firm A. T. Kearney (2010) estimates that India is the third among the top 25 inward FDI optimistic countries across the world. The report also observes that the investors have shown a strong vote of confidence for the strength of BRIC (Brazil, Russia, India and China) countries. Very recently the country has mooted the idea of CEO forums, as a second string of FDI friendly policy. The CEO forums can spearhead Track II diplomacy of the economic kind where in the high-level corporate interaction between two countries can create an enabling environment that could be capitalized wherever seemingly intractable bilateral hurdles crop up (Joshi, 2010).

India and China will retain their supremacy in this regard. Some policy prescriptions are put forward to cement the position of India as a global investment enabler. Such steps may include raising the cap limit, further liberalization of FDI in defense production, furtherance of automatic approval, liberalize the brown-field investment, overhaul of retail sector and more transparent governance and civil administration.

CONCLUDING COMMENTS

It has, ipso-facto, been proved that India is sustainable investment destination and the same has been reinforced by the sustained rise in the inward FDI flow to the country over the last twenty year span of time, signifying the growing degree of India's transationality (a measure of the relative economic importance of foreign affiliates in total economic activity; refer UNCTAD, 2005) and it will continue to surge in future also. The rapid strides in inward FDI can be cited as an important indicator of gains from structural economic reforms, underpinning the openness of the economy, reflecting the attractiveness of India as an investment destination. FDI is playing a decisive role in the infrastructure development in the country. It is widely known that the skepticism on the motive of foreign capital and heavy obsession on the principle of 'self-reliance' were the major impediments for the unimpressive growth FDI during the early stage of reform regimes. It is during the 1993-94 there seemed to be a realization of the importance of FDI. This enlightenment led to the progressive removal of barriers of foreign capital inflow through greater procedural simplifications and threshold limit. Now India provides a liberal, seemingly attractive and investor-friendly investment climate. The database on FDI we have discussed aforesaid is a solid evidence of recognizing its potential as an accommodative host for FDI. The major motivation of foreign investors to enter the Indian market is low-cost level of the skilled labour force and this decreasing cost advantages will be even more significant in the future. However, we are not overlooking the labour militancy and unrest, which is veritably a nightmare and strange industrial relation to foreign investors. The future of India's growth and output is seen to be connected to FDI and it was deemed necessary for promoting higher growth of output, exports and employment through enabling policy framework.

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