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   STATEMENT OF THE PROBLEM

   OBJECTIVES

   HYPOTHESES

   RESEARCH METHODOLOGY

   RESULTS & DISCUSSION

   FINDINGS

   RECOMMENDATIONS/SUGGESTIONS

   CONCLUSIONS

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- Bowersox, Donald J., Closs, David J., (1996), "Logistical Management." Tata McGraw, Hill, New Delhi.
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- Sharma T., Kwatra, G. (2008) Effectiveness of Social Advertising: A Study of Selected Campaigns, Corporate Social Responsibility, Edited by David Crowther & Nicholas Capaldi, Ashgate Research Companion to Corporate Social Responsibility, Chapter 15, pp 287-303.

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- Schemenner, R.W., Huber, J.C. and Cook, R.L. (1987), "Geographic Differences and the Location of New Manufacturing Facilities," Journal of Urban Economics, Vol. 21, No. 1, pp. 83-104.

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- Garg, Sambhav (2011): "Business Ethics" Paper presented at the Annual International Conference for the All India Management Association, New Delhi, India, 19–22 June.

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- Kumar S. (2011): "Customer Value: A Comparative Study of Rural and Urban Customers," Thesis, Kurukshetra University, Kurukshetra.

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RELATIONSHIP BETWEEN TRADE AND FDI: EVIDENCE FROM FOOD PROCESSING SECTOR IN INDIA

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ABSTRACT

Whether trade and FDI flows are complements or substitutes? Research is on and it has become a huge concern in FDI and Trade literature. The theoretical literature with respect to MNCs often assume that firms decide between supplying a foreign market through exports or tries to establish production facilities in a host country through FDI. The empirical evidence gives mix results, while some studies states that relationship between FDI and Trade are Substitute, on the other hand, some studies states that relationship between FDI and Trade are complementary. A vast amount of empirical literature has been developed with complement to the relationship between FDI and Trade as whole but the results on empirical linkages are inconsistent and ambiguous. This paper analyzes whether trade and FDI are substitute or complements with special reference to Food Processing Industry in India for the period 1991-2010.

JEL CLASSIFICATION
E-22, F-18, F-21

KEYWORDS
trade, FDI, food processing sector.

INTRODUCTION

India major player in the world: India is one of the most important producers of food products in the world. Indian food processing industry is raising its bar by up grading its link with the agricultural and industrial sector across the global economy. Agriculture sector with its associated sectors are playing pivotal role in policy to promote inclusive growth, enhance rural income and sustain food security.

High demand for Food Processing: Increasing number of nuclear families and working women, growing spending on health and nutritional foods, shifting demographics and rising disposable incomes has given a considerable push to the industry growth. A developed Food processing industry can improve the value and value chain of agricultural product/s; create stable prices to agricultural product and generates demand for Indian agricultural products in the world market. According to Ministry of food processing industry, "India is the second largest producer of food in the world next to China and the Indian food processing industry is one of the largest in terms of consumption, production, and trade prospects. Main activities in the food processing industry are Fruit and Vegetable processing, Grain processing, packaged food, Fish-processing, Beverages, Milk processing, etc. India has arable land of 184 million hectares and produces annually 105 million tones of milk, 150 million tones of fruits and vegetables, 485 million livestock, 230 million tones food grain, 7.0 million tones fish, 489 million poultry and 45 billion eggs. India's agricultural production base is huge. India ranks first in the world in production of cereals, livestock population and milk. It is second largest fruit and vegetable producer and is among the top five producers of rice, wheat, groundnuts, tea, coffee, spices, sugar and oilseeds. This gives it the unique advantage and tremendous potential for processing of agriculture produce. (Ministry of food processing industry, Annual Report 2008-09). However, processing level is very low for example around 2.20% in fruits and vegetables compared to countries like USA (65%), Philippines (78%) and China (23%); 35% in milk, 21% in meat and 6% in poultry products, as against 60-70 % in developed countries. India's share of processed food is about 1.6%. To facilitate the prompt growth of food processing industry, the government has implemented the scheme for infrastructure development comprising a food park scheme, establishing packaging centers, integrated cold chain facility, value added centers, Irradiation facilities.

35% food wastage due to lack of infrastructure: Food production in India is quite strong but at the same time wastage of agriculture produce is very high. Government is doing lot of work, activities and changes in policies for increasing the food processing sector but food processing industry is facing constraints like non-availability of adequate finance facility, infrastructural facilities like cold storage, warehousing, lack of adequate quality control & testing infrastructure, inefficient supply chain and involvement of middlemen, lack of process-able varieties of farm produce. India loses more than Rs. 50,000 crore (around 35% of total value) worth of agricultural food items due to lack of post harvesting infrastructure such as cold chains, transportation, and storage facilities. Indian agriculture is highly dependent on Monsoon, pre-harvest activities are natural we cannot control over these factors but we can make improvements in those factors which is in our hand, huge looses that we are making from these food wastages can be prevented by processing this food. India is losing lot of revenue by food wastages. (Annual Report 2008-09, Ministry of food processing industry)

Role of FDI: One of the most important factors that is affecting to food processing industry is non-availability of capital for investment. Moreover, capital inflows are of crucial importance for the restructuring of food processing industry in India. For the technological upgradation and modernization in the food processing units/ sector in India, a large amount of finance are required but local capital market is appearing to be not developed enough and adequate to make available of these funds. Hence, recently Government of India thought that Foreign Direct Investment (FDI) can be one the solution and source for this large scale of financial needs. FDI has immeasurable effects on the host country's economy. FDI increases the income, production, prices, employment, economic growth, development and general welfare of the recipient country. Therefore, FDI is a key element for successful economic growth in developing countries, because the very essence of economic development is the rapid and efficient transfer and adoption of "best practice" across borders. (Recap Kok & Erosy, 2009).An earlier trade theory explained by Ricardo in the early nineteenth century assumes immobility of production factors and it is based on comparative advantage. This theory explains that international trade is exclusively happening due to international differences in productivity of labor. According to Heckscher-Ohlin-Samuelson model, the basis for trade resided in the different relative factor endowment among countries. However, activities of MNCs are not explained in earlier models. The New trade theory began to incorporate models based on economies of scale, imperfect competition, barriers to trade and product differentiation. Then, models incorporating both trade and FDI have been acknowledged as horizontal and vertical where in the first type of such models FDI and trade proved to be substitutes while in the second complementary. FDI-Trade relationship also explained by demand and supply side models. Supply –side model explains that in the absence of barriers to market entry and decreasing returns to scale firms would decide to produce in a single low-cost location and supply final markets through trade rather than local production. Demand side model explains that as firm's foreign demand increases then it increases both FDI and export. Since the beginning of economic reforms in 1991, India has made a huge flow of FDI during the past two decades. India's considerable market potential and a liberalized policy regime have attracted more investment from foreign investors. With its constant growth performance and low-cost labor, India provides massive opportunities for investment. Major restructuring have been taken in the fields of financial sector, investment, trade, simplification in exchange control and its procedures, since the beginning of economic reforms in 1991. India provides a liberal, attractive, and investor friendly investment climate. Hence due to attractive climate, foreign direct investment in India increased from $ 4,361.4 million in 2005 to $ 27,099.7million in 2009. (SIA Newsletter, DIPP). From April 2000 to February 2010 Government of India get FDI of 5,110,055.69 Rs. Million. Out of this, the total amount of FDI for Food Processing Industries has been of 46,920.83 Rs. Million (0.96 % of the total foreign direct investment). Food Processing Industries Sector ranked 20th in the list of Sectors in terms of cumulative FDI approved from April 2000 to February 2010. (SIA Newsletter, DIPP)

LITERATURE REVIEW

THEORETICAL ISSUES WITH RESPECT TO LINKAGES BETWEEN FDI AND TRADE

One of the most important issues with respect to relationship between FDI and Trade is whether FDI increase or decreases the volume of trade. Theoretical literature with respect to FDI and Trade relationship explained that when FDI decreases the trade value, there is substitution relationship between FDI and trade, the major reason for this type of relationship is that MNCs set up subsidiaries abroad to supply local markets, instead of exporting. Alternatively when FDI increase the trade volume then there is complementary relationship between FDI and Trade, the major reason for this type of relationship is that MNCs relocate different stages of production in different countries. The substitutability and complementarily of properties of FDI with respect to trade are therefore often associated with horizontal and vertical FDI. Horizontal FDI is investment abroad at the same level of production, whereas vertical FDI is an investment in different stages of production.

HORIZONTAL MODELS OF FDI

FDI is horizontal when MNCs produces the same goods and services in different countries. When there is horizontal FDI then FDI substitutes for Trade FDI substitutes for Trade in horizontal FDI due to transaction cost in Trade in respect to transport barriers to trade and plant scale economies. As MNCs displace national ones, the volume of trade decreases, meaning that FDI substitutes trade.

VERTICAL MODELS OF FDI

FDI is vertical when MNCs split the production process across countries in order to reduce costs. This model is explained differences in relative factor endowments between countries which play a determinant role in explaining both trade and FDI.This particular model is explained by trade from developed to developing countries to exploit natural resources that is not available in host (developed) country. These investment are more likely to create intra-industry trade, by raising exports of capital equipment and factor services from the home country and exports of resource-based product from the host-country. MNCs tends to disperse the productive activities geographically and to centralize headquarter specific activities in a particular location, it lead to the creation of trade as well as FDI.

Generally, FDI and trade are referred as alternative strategies in the economic literature in the micro-level. There are different alternatives for firms, firms can produce at home and export or produce abroad and substitute foreign affiliates local sales for exports (Fontagne & Pajot 2002).Hence outward FDI may displace trade at the level of the firm, since foreign affiliates local sales substitute at least partly for exports. Overview of the theoretically documented relationship of FDI with International Trade flows is explained in table 3 taken from G. Zarotiadis and N. Mylonidis study (2005)**.** According Graham (1996) Complementary relationship between trade and FDI is explained through interlinkages of MNCs operations (demand for intermediate goods in home country) When the shareholder of MNC firm is from home country, the returns accruing to its foreign affiliates eventually accumulate to home country nationals through the parent organization. As foreign markets expand through income growth it is possible for both exports and foreign affiliate sales to grow together & thus benefit the home country.(Lipsey and Weiss). Malanoski et al. (1997) state that a firm with an increasing presence in a foreign country through FDI may be able to discover opportunities to export products from the home country that are not produced by their affiliates. Host country production and marketing staffs and distribution facilities could be used to find and service export customers in the host country and neighboring countries. Substitution relationship between trade and FDI is explained by Heckscher-Ohlin-Samelson (H.O.S), according the H.O.S theory when we relax the assumption of factor mobility then export and FDI turn into substitutes because as factor become mobile the differences in factor endowments between countries become smaller which has the effect of decreasing trade flows. FDI increases the number of units of capital in a host country by the same number of units of capital taken from home country. As a result of capital transfer, the factors of production in the home country fall leading to a decline in export hence there is negative relationship between FDI and exports.

SUBSTITUTION RELATIONSHIP BETWEEN FDI AND TRADE

If there is negative relationship between FDI and Trade, FDI is considered as displacing impact on trade. According to empirical studies, exports of the country are partially replaced by multinational enterprises (MNEs)' local sales in domestic market, unfavorable to the domestic industry's development. Reciprocally, home country's trade balance would benefit from this substitution effect, especially additional imports from the parent company are persuade Substitute relationship between FDI and Trade is found out by; Horstmann and Markusen, 1992 Ma et al (2000), Markusen and Venables, 1995). and Bayoumi and Lipworth (1997), while Graham (1999) finds substitution relationship between FDI and Trade for the USA. The new trade theory, building on imperfect competition, emphasises that economies of scale and transportation costs are key elements in this decision process. Increasing returns to scale limit the number of efficient plants, whereas transportation costs and more generally trade barriers act in the opposite direction. The so-called "proximity concentration trade off" (Brainard, 1993-a) is the key issue explaining if, and how, FDI substitutes for trade. Still, Helpman et al (2003) points out that this result may depend upon freight and tariff costs.

COMPLEMENTARY RELATIONSHIP BETWEEN FDI AND TRADE

If there is positive relationship between FDI and Trade, means Trade and outward FDI are complements then positive parameter is obtained in export (import) equation. Investing abroad leads to an increase in exports (imports) of country towards (from) the host country. Accordingly, an impact on countries trade balance should be positive or negative depending on whether exports increase by more than imports or not. Using time-series analysis, Andersen and Hainaut (1998) find complementary relationship between FDI and Trade: This study shows that there is different impact for different countries, for the United-States, Japan, and Germany this study found complementary relationship but not for the United Kingdom. Pfaffermayer (1996), Helpman, (1984). Brainard (1997) and Clausing (2000) for the U.S. and Co (1997) for Japan find that relationship between FDI and Trade are complementary. Using cross-sectional and time series industry-level data Pfaffermayer finds a significant complementary relationship between FDI and exports in the 1980's and early 1990's from Austrian manufacturing companies. According to Liu et al (2001) there is cyclical complementary relationship between trade and FDI using panel data approach.

MIXED (COMPLEMENTARY AS WELL AS SUBSTITUTION) RELATIONSHIP BETWEEN FDI AND TRADE

According to Pain and Wakelin, (1998) Outward investment has a generally negative impact on trade shares, while inward investment has a generally positive one. Hongshik Lee and Joon Hyung Lee (2007) shows that Trade and FDI have Substitution relationship if the affiliates are located in a developed country and mainly serve the host country, while there is complementary relationship between FDI and Trade if the affiliates export their products outside of the host country. Moreover, the complementary effect is strengthened if they are located in a less developed country. Blonigen (2001), examines product-level data for Japanese automobile parts for the US market, and finds substantial evidence for both a substitution and a complementarity effect between affiliate production and exports. Goldberg and Kein (1999) and Nakumara and Oyama (1998) find considerable evidence for the existence of both substitute and complementary relationship. Fukao et al (2003) scrutinize patterns of vertical intra-industry trade in East Asia and they find that the FDI in the particular region plays a significant role in enhancing the increase of the specific type of trade. Pantulu and Poon (2003) investigate that the relationship between outward FDI and exports is neither substitutes nor complements. Complementary and substation relationship between FDI and trade is different for different countries, industries and it is also depending on the time.

GAPS IN EXISTING LITERATURE

Previous empirical studies with respect to FDI and Trade are contradictory; and inconclusive regarding the specific question. The empirical evidence shows that sometimes FDI complements or substitutes trade. Relationship between trade and FDI is explained by various studies but there is still a lack of systematic study on the relationship between FDI and trade in food processing sector. What is the role of FDI in India's trade expansion of food processing products? Investigation of the linkage between FDI and trade growth would help us to reveal the major motives for investing in Indian economy which in turn might allow India's policy makers to take appropriate measures for stimulating further capital inflows and outflows

STATEMENT OF THE PROBLEM

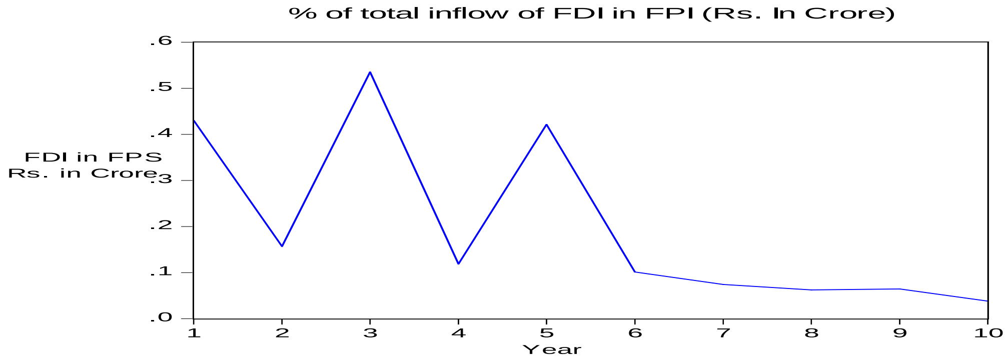
Though India has made significant policy reforms as India allowed 100% FDI through automatic route to attract more FDI in food processing industry, foreign direct investment in food processing industry in India is only 0.03 percent with total FDI approved in 2008-09. FDI in food processing industry is fluctuating over the last decade. Following diagram show the FDI in Food Processing Industry from 1999-00 – 2008-09 as compare to total inflow of FDI in India.

TABLE 1: INFLOW OF FOREIGN DIRECT INVESTMENT (FDI) IN FOOD PROCESSING INDUSTRIES SECTOR IN INDIA FROM 1999-2009 (Rs. In Crore)

Year	Total inflow of FDI in Food Processing Sector (Rs. In Crore)	Total inflow of FDI (Rs. In Crore)	% of total inflow of FDI in FPI (Rs. In Crore)
1999-00	444.06	103107.97	0.430674758
2000-01	198.13	126451.93	0.156684046
2001-02	1036.12	193608.25	0.535163145
2002-03	176.53	149322.85	0.118220353
2003-04	510.85	121173.55	0.421585404
2004-05	174.08	171378.73	0.101529519
2005-06	182.94	246127.37	0.07432737
2006-07	441	706300.62	0.062438003
2007-08	632	986643.94	0.064055529
2008-09	462	1230248.8	0.037553379

Source:SIA Newsletter, Department of Industrial Policy & Promotion, Ministry of Food Processing Industries, Govt. of India

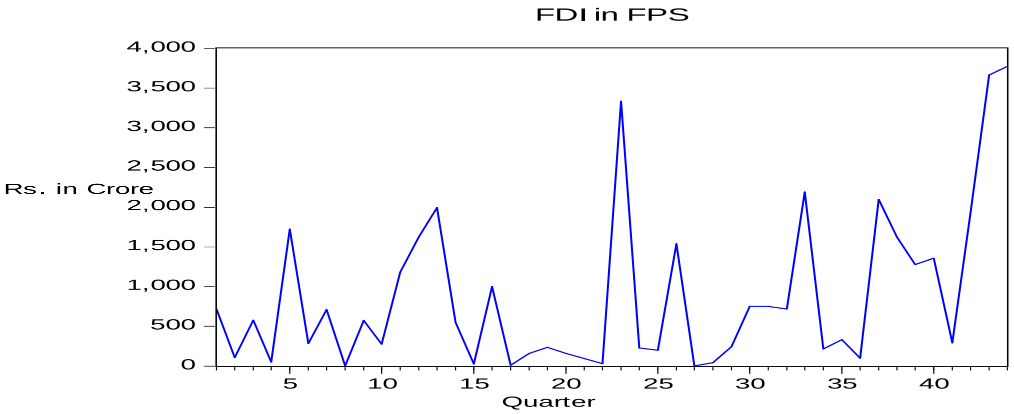
FIGURE 1: PERCENTAGE OF TOTAL INFLOW OF FDI IN FOOD PROCESSING SECTOR



Source: SIA Newsletter, Department of Industrial Policy & Promotion,

Also there are many fluctuations in quarterly inflow of FDI in food processing sector.

FIGURE 2: QUARTERLY FDI INFLOW IN FOOD PROCESSING SECTOR IN INDIA (FROM Q-1 1999 TO Q-4 2009)



Source: SIA Newsletter, Department of Industrial Policy & PromotioN

The above figure shows that there are many fluctuations in quarterly inflow of FDI in food processing sector.

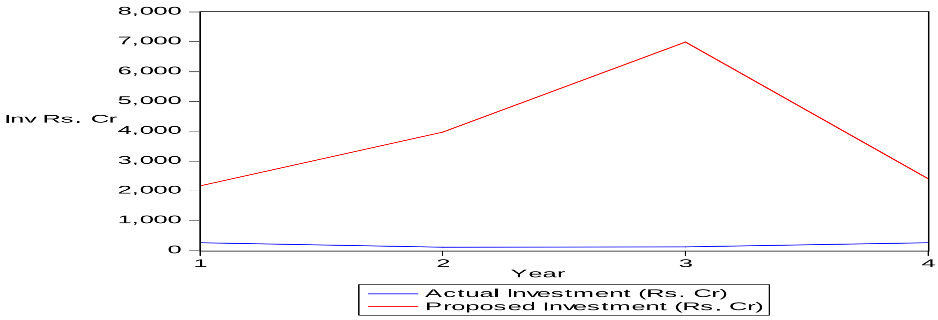
Also if we see the proposed Industrial Entrepreneurs Memorandum and implemented Industrial Entrepreneurs Memorandum in food processing sector, there is huge gap. Industrial Entrepreneurs Memorandum format is used for submission to the Central Government in the Secretariat for Industrial Assistance, for the purpose of record, a memorandum under the Industries (Development and Regulation) Act, 1951.This is shown by following table:

TABLE 2: IEMs FIELD AND IMPLEMENTED IN FOOD PROCESSING SECTOR FROM 2007 TO APRIL 2010

Year	Investment Intentions in Terms of IEMs Field	IEMs Implemented in FPI	Proposed Investment	Actual Investment
2007	87	54	2170	263
2008	123	18	3967	113
2009	157	48	6996	119
2010(Apr)	62	15	2409	260

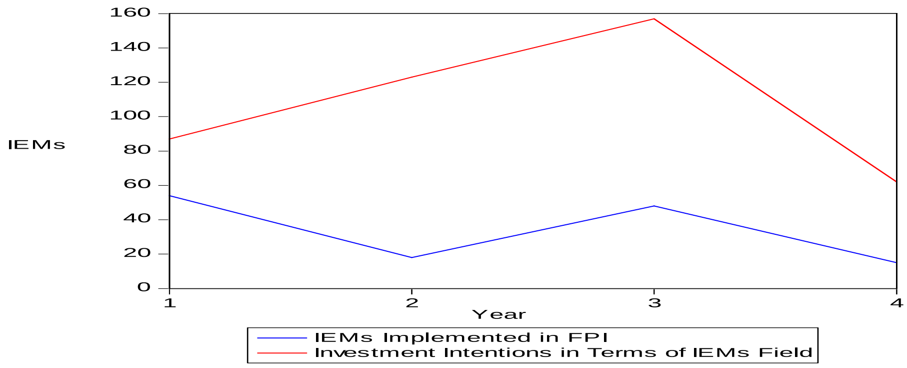
Source: SIA Statistics, Department of Industrial Policy and Promotion

FIGURE 3: PROPOSED AND ACTUAL INVESTMENT AS PER IEMS FIELD AND IMPLEMENTED IN FOOD PROCESSING SECTOR FROM 2007 TO APRIL 2010



Source: SIA Statistics, Department of Industrial Policy and Promotion

FIGURE 4: INVESTMENT INTENSIONS IN TERMS OF IEMS FIELD AND IEMS IMPLEMENTED IN FOOD PROCESSING SECTOR FROM 2007 TO APRIL 2010



Source: SIA Statistics, Department of Industrial Policy and Promotion

Above figure shows that there is huge difference between Investment Intensions in terms of IEMs Field and IEMs implemented and Actual Investment and Proposed Investment.

EXPORT OF FOOD PRODUCTS

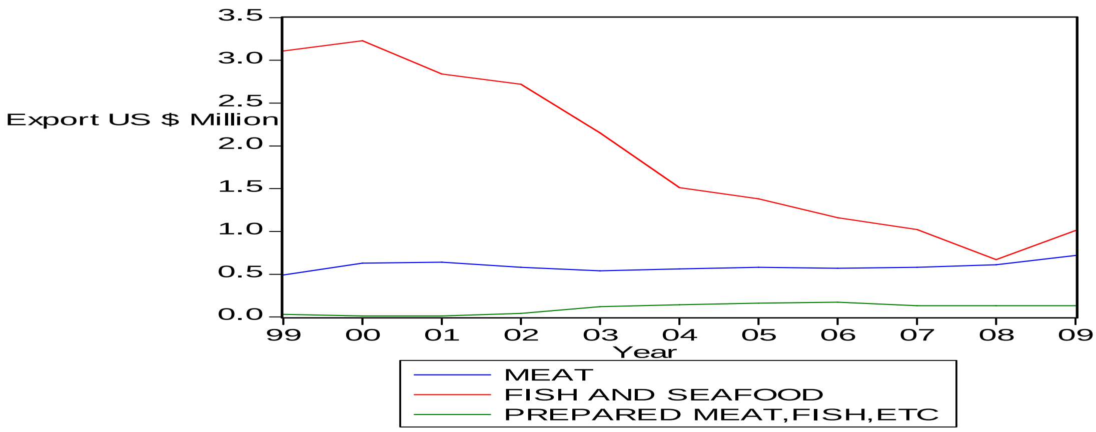
Though India has good production base in food the overall export of food products is decreasing with compare other products to world. The export of some important food products from India are shown by following Table,

TABLE 3: EXPORT OF MAJOR FOOD PRODUCTS FROM INDIA (US $ MILLION) FROM 1999 TO 2009

Year	Cereals	Fish And Seafood	Meat	Vegetables	Preserved Food	Prepared Meat,Fish,Etc	Live Trees And Plants	Baking Related	Edible Fruit And Nuts
1999	926.984	1100.46	174.4	200.13	43.4698	8.94225	27.6402	29.2953	691.847
2000	641.855	1364.23	267.468	252.098	52.9111	5.23004	25.3075	36.5418	607.623
2001	896.817	1231.05	274.983	234.08	70.9466	4.49608	26.0051	45.9503	540.989
2002	1278.32	1340.16	287.816	246.736	58.5485	19.4067	35.4346	56.5875	576.438
2003	1354.27	1235.29	308.459	275.07	75.1409	69.1982	43.4859	62.1433	519.411
2004	1811.35	1139.5	421.426	352.611	92.8649	108.696	54.8147	79.5977	683.201
2005	2053.41	1376.43	580.63	533.548	136.86	157.128	67.0023	116.913	870.541
2006	1593.19	1401.34	696.026	608.802	194.298	209.997	89.1393	127.807	857.764
2007	2794.79	1502.51	849.727	605.504	199.208	192.779	94.8432	156.134	867.364
2008	3995.58	1307.22	1181.6	681.849	267.457	246.994	82.7708	238.084	1135.81
2009	2975.21	1672.52	1184.04	817.471	264.45	214.089	65.7847	209.673	1037.84

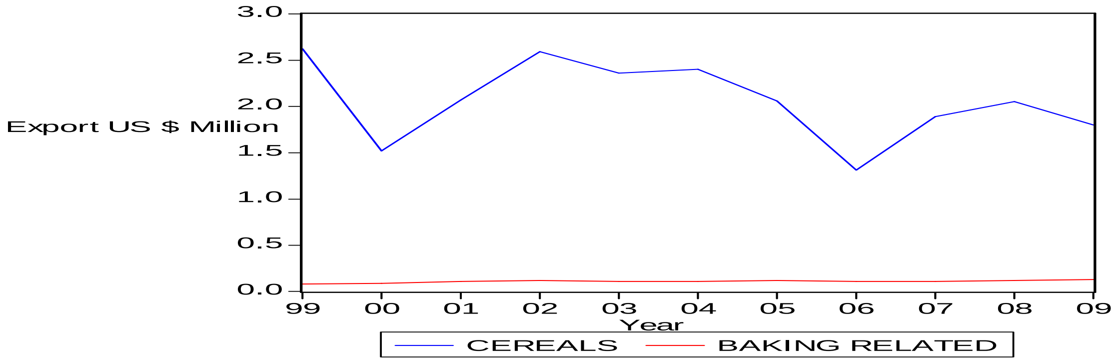
Source: DGCI&S, Ministry of Commerce

FIGURE: 5 PERCENTAGE SHARE OF MEAT (02), FISH AND SEAFOOD (03) AND PREPARED MEAT, FISH ETC (16) IN EXPORTS OF INDIA TO THE WORLD BETWEEN 1999-2009



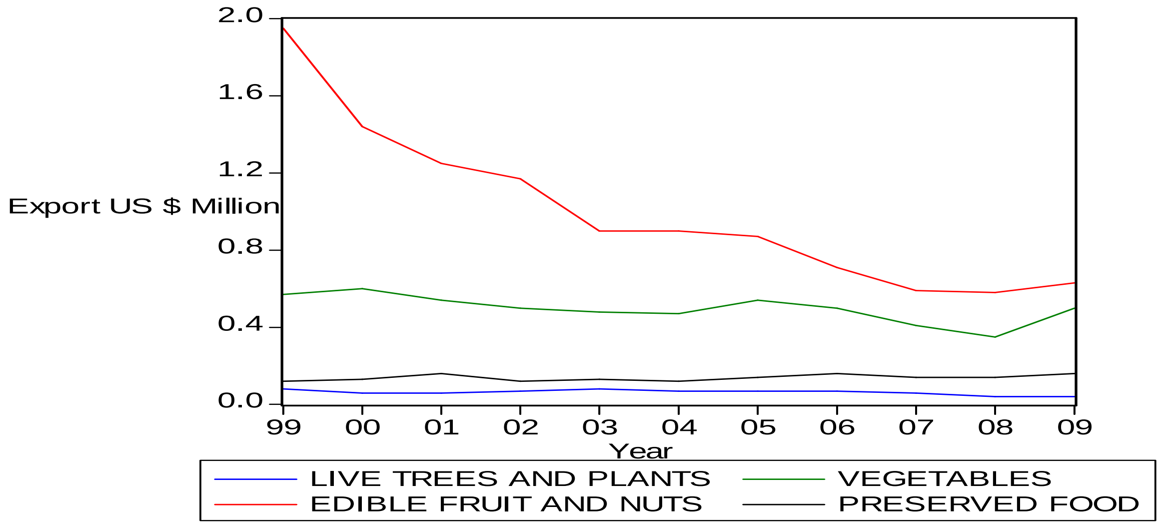
Source: DGCI&S, Ministry of Commerce

FIGURE: 6 PERCENTAGE SHARE OF CEREALS (10) AND BAKING RELATED PRODUCTS (19) IN EXPORTS OF INDIA TO THE WORLD BETWEEN 1999-2009



Source: DGCI&S, Ministry of Commerce

FIGURE 7: PERCENTAGE SHARE OF LIVE TREES AND PLANTS (06), VEGETABLES (07), EDIBLE FRUIT & NUTS (08) AND PRESERVED FOOD (20) IN EXPORTS OF INDIA TO THE WORLD BETWEEN 1999-2009



Source: DGCI&S, Ministry of Commerce

As we can see from above graphs there is decreasing trend of export in major food products from in India to world from 1999-2009. It can be summarized from above figure that one of the reasons for this decreasing trend is non-availability of capital for investment in food sector in India.

OBJECTIVE AND SCOPE

1. Analysis of trade flows in food processing sector in India for the period 1991-2010.
2. Analysis of FDI flows in the food processing sector in India for the period 1991-2010.
3. Relationship between FDI and Trade (whether FDI and Trade are complementary or substitutes with special reference to Food Processing Industry in India)
4. Relationship between FDI & Trade will be identified by simple regression model, FDI= B1 + B2 Trade+ r with separate equation for Inward FDI and Outward FDI and their relationship with Export & Import of food processing sector in India.
5. Examine the relationship between FDI and trade (whether positive or negative) and implications of the same. In other words, if FDI and Trade are substitutes, does it imply steps for trade restriction to increase the inflow of FDI in the food processing sector? If so, is it the correct approach?

METHODOLOGY

ESTIMATION FRAMEWORK

As discussed in the literature review, relationship between FDI and Trade are contradictory one, showing complementary, substitution and mixed results. Furthermore, these effects emerge at different levels of aggregation. Swenson (2004) states that trade needs to categorize into import and export to check the relationship between FDI and Trade because FDI affect differently to import and export. This paper only try to find out relationship between FDI and export of food processing sector as the data for import of food processing product is not available.

A regression specification that evaluates the effect of total FDI inflow on export for the time period 1991-2009(t).

ΔExport i = β1 Total FDI inflow $_{t-1}$+ e

Where ΔExport and measure changes in the India's exports of food processing products. I had taken changes in India's exports of food processing products to avoid non-stationarity as it is time series data. Total FDI inflow is total FDI inflows in food processing sector in India. Whether FDI inflows effects are positive or negative with respect to export is a question to be resolved through empirical analysis.

DATA SOURCES

All data on total FDI inflow for regression is taken from SIA Newsletter, DIPP (Department of Industrial Policy and Promotion) database for the period 1991-2010.Data on export of food processing sector is taken from DGCIS.

EMPIRICAL FINDINGS

Simple linear Regression Model is used to identify coefficients or multipliers that describe the size of the effect the independent variables on dependent variable.

Dependent Variable: TRADE

Method: Least Squares

Date: 01/30/11 Time: 18:05

Sample: 1 18
Included observations: 18

Variable	Coefficient	Std. Error	t-Statistic	Prob.
FDI	9.831065	3.519085	2.793642	0.0130
C	2703.960	1554.394	1.739559	0.1011

R-squared	0.327856	Mean dependent var	5966.101
Adjusted R-squared	0.285847	S.D. dependent var	5150.803
S.E. of regression	4352.817	Akaike info criterion	19.69947
Sum squared resid	3.03E+08	Schwarz criterion	19.79840
Log likelihood	-175.2953	Hannan-Quinn criter.	19.71311
F-statistic	7.804438		
Prob(F-statistic)	0.013011		

From the simple regression model of export of food processing sector on inward FDI in food processing sector, R-squared is 0.32, which shows that the model explains 32% variation in export of food processing sector in India. The F statistics is 7.08, and the probability of F statistics is 0.01 which shows that the results are statistically significant and the null hypothesis of the independent variables having no effect on Total export of food processing products from India is rejected.

The above table shows that the coefficient of inward FDI in food processing sector in India is positive which implies that the inward FDI has positive effect on total export. The probability value associated with t statistics of this coefficient is 0.01 which is less than 0.05 which shows that the estimated value of the coefficient of inward FDI in India is statistically significant. Results show that 1% increase in inward FDI in India around 9.83% export food processing products of India.

CONCLUSION

Empirical findings show that there is complementary relationship between outward FDI and export of food processing sector. Overall Results shows that inward FDI is promoting exports of food processing sector. Results show that 1% increase in inward FDI in India around 9.83% export food processing products of India.

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