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Trends of FDI Inflow in India

Dr. Vikramjit Singh
Associate Professor
Department of Political Science
Dayanand College, Hisar (Haryana)

Abstract

The most essential element for the growth of economy of the nation depends on availability of capital for the investment in different sectors. The developing nations are struggling for economic growth due absence of abundance of capital. India is also not exception to it. Although India has abundance of natural resources but it lacks capital to exploit these resources. Like other developing nations India needs huge capital to invest to develop its economy and the nation. Foreign Direct Investment (FDI) is one of the richest forms of capital for developing nations to develop their economies. The developed nations use to invest directly in developing nations and such investment is very fruitful to extend their economic activities and for growth. Soviet Union was not only a good friend of India but also provided a great economic assistance to develop and extend economic activities of India but with the disintegration of Soviet Union India lost not only a formidable supporter in international politics but also strong economic supporter. In this changed world economic scenario European Union emerged as one of alternate for India to envisage its economic activities in future.

Demise of Soviet Union brought a sea change in international politics. The whole world has started economic realignment in changed economic situation. India lost a good friend and formidable supporter in form of Soviet Union. It not only supported India in world politics but it provided huge financial assistance to grow Indian economy and now India had to realign its economy with new economic partners. New economic reforms were launched by Government of India in 1991 which opened Indian economy to the world and in this light India has to search new economic partner which could fulfil the demands of fast growing economy of India. European Union could be the most suitable alternate for in this situation because it is one of the most powerful economic and political unions of 28 countries of Europe with a combined population of over 500 billion people or 7.3 per cent of the world population. The combined GDP of EU is 17.6 trillion US$ in 2011 representing nearly 20 per cent of the global GDP when measured in terms of purchasing power parity. EU traces its origin from the European Coal and Steel Community (ECSC) and the European Economic Community (EEC) formed by six founding members in 1951 and 1958 respectively. After sixty years of its formation, the membership of EU has reached 28 with Croatia as last member to join in July 2013.

The EU as a bloc of 28 countries is India's largest trading partner and one of the largest sources of FDI. Both are in the process of negotiating a bilateral broad-based trade and investment agreement since 2007 which was aimed at to enhance the commercial relationship.

In the changed world scenario which is the witness of increasing globalization, liberalisation and privatisation and the economic, political, and other barriers are rapidly disappearing and whole has shrunk to village and the nations have to be very competitive in this village to survive. Foreign Direct Investment (FDI) can be considered as an viable economic strategy and the developing nations who are the seekers of FDI have to create the conditions viable to foreign investment. The inward FDI depends to a certain extent on the step which a country or a group of countries have reached in investment development path paradigm. The economic reforms launched in 1991 in India is a step forward to attract the foreign investors in India. The EU appears as the most important foreign direct investor and it reveals the ability and tendency of their firms to internationalize business activities. In the fast growing markets of India, however, the share of EU firms in total FDI is rather low and not particularly dynamic. Foreign direct investment has become the major pillar of internationalization of economic activities of their firms, yet its global FDI flows are still much lower than trade flows. Firms undertake FDI primarily in order to expand and compete with domestic and other firms in the irrespective markets. Some other factors like perception of country and risk found are to be decisive factor for FDI in emerging markets.

Trends and Patterns of FDI Inflows in India

Table 1: FDI Inflows in India (August 1991-March 2013) (US$ million)

Year	Amount of FDI Inflows
1991-92	129
1992-93	315
1993-94	586
1994-95	1314
1995-96	2144
1996-97	2821
1997-98	3557
1998-99	2462
1999-00	2155
2000-01	4029
2001-02	6130
2002-03	5035
2003-04	4322
2004-05	6051
2005-06	8961
2006-07	22826
2007-08	34835
2008-09	41873
2009-10	37745
2010-11	34847
2011-12 (P)	46556
2012-13 (P)	36860

Note: Data for 2011-12 and 2012-13 are provisional.
Source: Secretariat for Industrial Assistance, FDI Fact Sheets, 1991 – 2013.

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Trends and patterns of FDI inflows in India during the post-liberalization has well explained by the statistics given in the table 1 given below: FDI inflows in India was recorded to $129 million, which had tremendously increased to the level of $315 million, with 144 per cent annual growth rate in 1992-93 over the previous year. In 1993-94, a growth rate of 86 per cent was recorded in FDI inflows over 1992-93 and reached to the level of $586 million. FDI inflows in India increased considerably in 1994-95 and reached to $1314 million, with 124 per cent annual growth rate.

FDI inflows increased from the level of $129 million in 1991-92 to the level of $2144 million in the year 1995-96, with a growth rate of 63 per cent over 1994-95. During the period from 1991-92 to 1995-96 the average FDI inflows had amounted to $898 million and recorded average annual growth rate of 83.52 per cent. During the period from 1991-92 to 1995-96, the highest FDI inflows in India had amounted to $2144 million in 1995-96, whereas the highest annual growth rate of 144 per cent was recorded in 1992-93. The increase was largely due to the expanded list of industries or sectors which were opened up for foreign equity participation. However, through the new economic policy and the new industrial policy of 1991, a series of policy measures were announced to liberalize the FDI environment in the country.

Policy towards foreign investment was liberalized in 1991 to permit automatic approval for foreign investment up to 51 per cent equity in 34 industries. The foreign investment promotion board was also established to process applications in cases, which were not covered by automatic approval. During 1992-93 several measures were taken to encourage investment flows in the economy through FDI, portfolio investment, NRI investment and deposits and investment in global depository receipts. FDI has been allowed in exploration, production and refining of oil and marketing of gas. Under the new industrial policy of July 1991, approvals for FDI up to 51 per cent of equity in specified high-priority industries were given automatically subject to the condition that the dividend payments should be balanced by export earnings over a specified period of time.

During 1996-97, FDI inflows increased to $2821 million, with 31.6 per cent annual growth rate over the previous year. In the next year, a growth rate of 26.1 per cent was recorded in FDI inflows and reached to the level of $3557 million in absolute terms. During the period from 1991-92 to 1997-98, the total amount of the FDI inflows had amounted to $10866 million and it was found that there had been a continuous increase in FDI inflows. The Foreign Investment Promotion Board (FIPB) had permitted FDI in the area of financial services in 1997-98. During 1998-99, FDI inflows in India declined to $2462 million by 30.8 per cent annual growth rate and it was found that FDI inflows had declined for the first time since 1991-92 due to unfavorable international economic environment.

There was a decline in FDI inflows from $2462 million during 1998-99 to $2155 million (12.5 per cent decrease) during 1999-2000 which could be partly on account of sluggish domestic investment demand. The most important reasons for the declining trend included several restrictions imposed on India by the USA on account of the nuclear test carried out by India at Pokhran, the political instability, slowdown of the Indian economy, the restrictions imposed on the FDI inflows regarding Trade Related Investment Measures (TRIMS), the poor domestic industrial environment and the unfavorable external economic factors such as the financial crisis of South-East Asia. A number of FDI policy initiatives were taken in the year of 1999-2000 to further facilitate inflows of FDI in India. In August 1999, Foreign Investment Implementation Authority (FIIA) was set up for speedy conversion of approvals to actual flows.

In 2000-01, FDI inflows in India increased to the level of $4029 million with 87 per cent annual growth rate over the previous year. The share of equity capital, re-invested earnings and other capital was $2400 million, $1350 million and $279 million respectively in total FDI inflows. The Gujarat earthquake (January 2001), the terrorist attack on the Indian Parliament (December 2001), and the terrorist attack on the World Trade Centre (WTC) (September 2001) brought about a temporary dislocation in FDI inflows in India. Table 4.1 reveals that during the period from 1996-97 to 2000-01, average annual growth rate of 20.28 per cent was recorded and average FDI inflows had amounted to $3005 million, which was 3.35 times greater than average FDI inflows from 1991-92 to 1995-96. The highest FDI inflows of $4029 million and the highest annual growth rate of 87 per cent were recorded in 2000-01. Hence, it may be concluded that equity capital component of FDI inflows was the sole component of FDI inflows till 2000-01.

In the year 2001-02, FDI inflows in India increased to the level of $6130 million, a growth rate of 52 per cent was recorded over the previous year. This was due to liberalization of the FDI policy. The inflows of the FDI decreased to the level of $5035 million (decrease of 17.9 per cent) in 2002-03, which further declined to $4322 million (decrease of 14.2 per cent) in 2003-04. The overall decline in 2002-03 and 2003-04 was principally due to the sharp fall in the net equity inflows through SIA/FIPB route mainly in electronics, electrical and service sector. It reveals that the share of equity capital, re-invested earnings and other capital was $2229 million, $1460 million and $633 million respectively in total FDI inflows in 2003-04. FDI inflows grew steadily through the first half of the 90s but stagnated between 1996-97 and 2003-04. The year-on-year fluctuations until 2003-04 make it difficult to identify a clear trend.

During 2004-05, FDI inflows in India increased by 40 per cent and reached to the level of $6051 million in absolute terms. FDI inflows in India had amounted to $8961 million in absolute terms, which were increased by 48 per cent during 2005-06 on the back of positive investment climate, improved growth prospects and initiatives aimed at rationalizing and liberalizing the FDI policy and simplifying the procedures. The average FDI inflows in India from 2001-02 to 2005-06 had amounted to $6100 million which was 2.03 times greater than average FDI inflows from 1996-97 to 2000-01 and recorded an average annual growth rate of 21.62 per cent. The highest FDI inflows of $8961 million were recorded in 2005-06, while the highest annual growth rate of 52 per cent was recorded in 2001-02. In view of bringing the FDI compilation of India, in line with international best practices, coverage of data on FDI has been expanded from 2000-01 by including certain new items, viz., equity capital of unincorporated bodies, reinvested earnings and inter-corporate debt transactions between the related entities.

Table 2: Cumulative Countries-wise (EU) FDI inflows in India (1991- 2000)

Rank	Country	Amount of Inflows (US$ million)	Share as % of total Investment
1	Germany	746.60	5.28
2	Netherlands	735.04	5.20
3	U.K.	722.42	5.11
4	France	350.04	2.47
5	Switzerland	277.08	1.96

Source: SIA News Letter, Issues, 1991 – 2000.

India opened its economy for direct investment in 1991 but till 1995 the response of European countries was not very impressive because they were hesitant to invest in India due to

Principal
Dayanand College
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sluggish economic growth and close economy and it was just the beginning of liberalization process in India. But a landmark development can be seen in 1995 with the economic integration of Europe in the form of European Union. The Main investors of European Union from 1995 to 2000 in Indian markets were Germany, Netherland, UK, France and Switzerland and that can be seen in the given table 2 given below.

The EU is India's most important trading partner while the later is a top-10 trade destination of former. Nonetheless, the levels of trade value and FDI between the EU and India are still relatively small. However, there is fast increase in trade and FDI flows between the EU and India, which suggests the latter is going to become more strategic for the former in the years to come. This, however, is not a uniform pattern with all the states of the EU, rather top five FDI sending EU countries are Germany, Netherlands, UK and France. Germany ranked the 4th in top ten source countries investing in India and 1st in the EU countries with a share of 5.28 per cent in total FDI inflows in India. Netherlands ranked 5th in top ten source countries and 2nd in the EU countries with a share of 5.2 per cent in total FDI inflows. Likewise, UK ranked 6th and France ranked 9th in top ten countries investing in India and 3rd and 4th rank in the EU countries with a share of nearly 5.11 per cent and 2.47 per cent respectively in total FDI inflows. During the same period Switzerland FDI inflow was 277.08 US million $. The share of the rest of the members of EU was negligible during this period.

Table 3 Total FDI Inflow and from EU (2000-2011) (US$ million).

Calendar Year (January-December)	Total FDI Inflow in India	FDI Equity Inflows from EU	% of Total
2000	4029	574.78	23.67
2001	*6130	1005.87	28.17
2002	5035	823.94	24.51
2003	4322	657.86	31.64
2004	6051	1056.06	32.87
2005	8961	664.58	15.26
2006	22826	2927.75	26.33
2007	34835	2444.55	15.35
2008	41873	6258.99	16.87
2009	37745	4562.87	16.72
2010	34847	4522.21	21.53
2011	46556	15260.09	44.01

Note: 1. * These amounts include the inflows received through FIPB/SIA route, acquisition of existing shares, RBI's automatic route & RBI's – NRI schemes.

2. The amount of FDI equity inflows, in respect of country/sector specific data was not provided by RBI, Mumbai, prior to January 2000.

Source: SIA News Letters, 2001 – 2012.

FDI Inflows in India from EU Countries

Table 3 shows year-wise FDI inflows received from EU companies with percentage share of total, since January, 2000, as compared to total FDI equity inflows. In year 2000, FDI equity inflows from EU companies amounted $574.78 million which is 23.67 per cent of total FDI inflows. The EU-India relations became institutionalized with the staring of summit meetings which first took place in Lisbon, Portugal on 28th June, 2000. In this meeting both agreed to build a new strategic partnership founded on shared values and aspirations characterized by enhanced and multifaceted cooperation. Also, the joint declaration of the first summit gave the new concept of strategic partnership oriented toward 21st century.

In the year 2001, the share of EU companies increased to 28.17 per cent which again declined in 2002. The second summit meeting between EU and India took place in New Delhi on 23rd November, 2001. This meeting saw a tacit understanding of India's point of view on the issues of cross border terrorism, trade and investment particularly FDI. The year-wise FDI inflows show a fluctuating trend and it is found that during January, 2000 – December, 2011, the highest share of EU companies in total FDI inflows is 44.01 per cent in 2011 and the lowest share is 15.26 per cent in 2005. The cumulative FDI equity inflows received during January, 2000 – December, 2011 is US$ 165813 million. Out of this, FDI inflows from EU are US$ 40759.55 million, which represents 24.58 per cent of the cumulative inflows received. Therefore, an analysis of the FDI equity inflows, received in India, since 2000, shows that the FDI equity inflows have increased substantially. There can be seen a major growth in FDI inflow both from EU and world in 2010 two FDI inflow from EU was 4522.21 Million US Dollar which rose up to 15260.09 06 Million Dollar. In 2010 world inflow was 34847 Million Dollar which rose to 46556 06 Million Dollar. This table indicates when there in major change in FDI the change is in both European Union in the world.

Table 4: Top 5 EU Countries Investors in India.

Rank	Country	Cumulative FDI Inflows, (2000-2011); Rs. Million	Share of FDI Inflows (percent)
1	United Kingdom	780279.08	35.76
2	Netherlands	396633.28	18.18
3	Cyprus	318423.70	14.59
4	Germany	236171.20	10.82
5	France	159573.40	7.31
Total EU Countries		2181813.77	100

Source: SIA News Letter, Issues, 2000 – 2012.

Although India has liberalized the regime for FDI, it remains restricted in a couple of sectors, such as banking services and telecommunications. Restrictions remain, particularly in the services sector, which includes financial and banking services, despite of their importance in attracting FDI to India. The Table 4 shows statement of FDI inflows for EU countries from January 2000 to December 2011 and total period is divided into two sub-periods of 2000-05 and 2006-12 and countries ranking is made on the basis of total investment made in India. It shows that the list of investing EU countries to India reached to maximum number of 24 in 2011 as compared to 15 in 2000. Although, India is receiving FDI inflows from a number of sources but large percentage of FDI inflows is vested with few major countries. During the period 2000-05, nearly 25.16 per cent FDI inflows recorded from EU countries. This share declined to 24.51 per cent during 2006-2012. Therefore, it is found that the overall share of EU countries in total FDI inflows in India slipped down to 24.58 per cent during 2000-11.

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Sector-Wise Distribution of FDI Inflows in India from EU Countries
Table 5: Share of Top Sectors attracting FDI Equity Inflows from EU
(From January, 2000 to December, 2011)

Rank	Sector	Amount of FDI equity inflows (US$ million)	% age of FDI equity inflows from EU
1	Chemicals (other than fertilizers)	6486.61	15.91
2	Services Sector*	6282.90	15.41
3	Construction Development: Township. Housing, Built-up infrastructure and construction development projects	3611.36	8.86
4	Drugs & Pharmaceuticals	2895.93	7.10
5	Automobile Industry	2824.16	6.93
Total of Above		22100.96	54.21

Note: * Services sector includes Financial, Banking, Insurance, Non-Financial/Business Outsourcing, R&D, Courier, Tech. Testing and Analysis, others.
Source: SIA Newsletter, 2000 – 2012

On perusal of the sector-wise distribution of FDI equity inflows received from EU, it is seen that the highest inflows have been in the chemicals (other than fertilizers), which accounts for about 16 per cent of total inflows. Services sector, which receives the share of over 15 percent comes to second place, construction development with about 9 per cent is in third place, drugs & pharmaceuticals with over 7 per cent is in fourth place and automobile industry with 6.93 per cent is in fifth place. Thus, nearly 54.21 percentages of inflows received from EU countries in top five sector of India.

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