LIBERALIZATION AND FDI TRENDS IN INDIA

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Since Independence till 1990, the performance of Indian economy has been dominated by multiple controls, restrictive regulations and wide ranging State intervention. Industrial economy of the country was protected by the State and shielded from external competition. In the year 1989-90, the situation on the balance of payment and foreign exchange reserves became shaky and the country was driven to the threshold of default. The credibility reached the sinking level, and that no country was willing to advance or lend to India to tide over the situation. From that period onwards the government followed a liberalized economic policy in July, 1991. The Government has taken a series of measures like devaluation of rupee, lowering of import duties and allowing foreign investment up to 51 per cent of the equity in a large number of industries and investment of large foreign equity even up to 100 per cent in selected areas especially for export oriented products[1].

In the 1980s, FDI was concentrated within the Triad[2] i.e., EU, Japan and the US. However, in 1990s, the FDI flows to developed countries declined, while those to developing countries increased in response to rapid economic growth and fewer restrictions. The growth of FDI flows to developing countries is unevenly distributed among regions and groups of developing countries. Small markets with low growth rates, poor infrastructure, high indebtedness, slow progress in introducing market and private sector oriented economic reforms and low levels of technological capabilities are not attractive to foreign investors.

MEANING

The term Foreign Direct Investment refers to any investment in a foreign country where the investing party retains control over investment. It can be inbound or outbound[3.] The Pepsi Company is a case of Inbound FDI and Tata buying JLR is a case of Outbound FDI. Net of Inbound and Outbound FDI in a country will give a net FDI informs in the country. The Government of India has put in place a liberal policy on FDI, under which FDI up to 100 per cent is permitted under the automatic route in most sectors/activities. The policy is reviewed on an ongoing basis, with a view to making it more investor-friendly. Significant changes have been made in the FDI policy regime in recent times to ensure that India remains an increasingly eye-catching investment destination. The Department of Industrial Policy and Promotion plays an active role in the liberalization and rationalization of the FDI policy.

Sectors prohibited for FDI

It is prohibited in "Lottery business including Government/ Private lottery, online lotteries, Gambling and Betting including casinos, Business of Chit Fund, Nidhi Company, Trading in Transferable Development Rights, Real Estate Business or Construction of Farm Houses, Manufacturing of Cigars, Cheroots, Cigarillos and Cigarettes, of tobacco or of tobacco substitutes and Activities/Sectors not opened to private sector investment including Atomic Energy and Railway Transport (other than Mass Rapid Transport Systems)"[4.]

Improvement of FDI

In connection with the improvement of FDI scenarios in the country, the Government has introduced various measures for liberalization/rationalization of FDI policy in terms of various circulars and Press Note 1 to 9 of 2012[5.] Some of the important policy measures includes FDI in single brand retail trading, mandatory approvals under FDI schemes, investment by banking companies in their subsidiaries, joint ventures and associates, permitting a citizen of Pakistan or an entity incorporated in Pakistan to make investments in India, under the Government route, in permitted sectors/activities, other than defence, space and atomic energy, conditions relating to single brand retail trading, FDI permission up to 51 per cent under the Government route, in Multi-Brand Retail Trading subject to fulfilling certain conditions, FDI in civil aviation sector, Broadcasting Sector, Power Exchanges registered under the Central Electricity Regulatory Commission Regulations 2010 and setting up to step-down subsidiaries for specific NBFC activities were taken into account which is mainly based on the prevailing circumstances.

Calculation of Foreign Investment

Investment in Indian companies can be made both by non-resident as well as resident Indian entities. Any non-resident investment in an Indian company is direct foreign investment. Investment by resident Indian entities could again comprise of both resident and non-resident investment. Thus, such an Indian company would have indirect foreign investment if the Indian investing company has foreign investment in it. The indirect investment can also be a cascading investment i.e., through multi-layered structure. For the purpose of computation of Indirect Foreign Investment, Foreign Investment in Indian company shall include all types of foreign investments i.e., FDI, investment by FIIs, NRIs, ADRs, GDRs, Foreign Currency Convertible Bonds fully compulsorily and mandatorily convertible preference shares and fully compulsorily and mandatorily convertible Debentures regardless of whether the said investments have been made under Schedule 1,2,3 and 6 of FEM (Transfer or Issue of Security by Persons Resident Outside India) Regulations, 2000[6].

FDI and External Loans

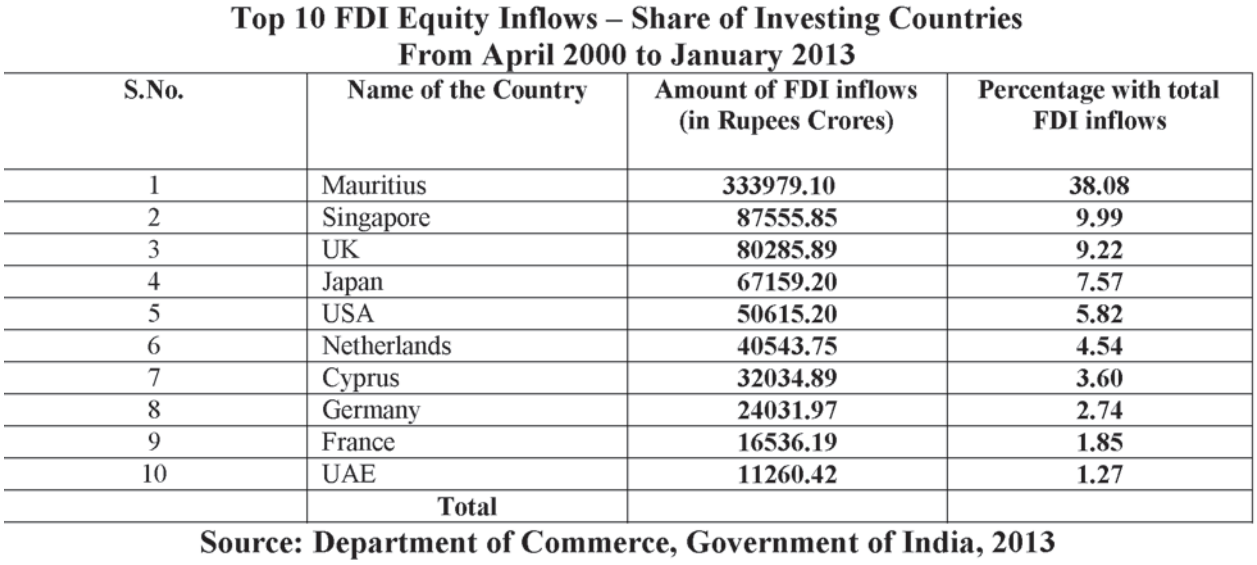
FDI takes the form of repatriation of a certain percentage of earnings in the form of dividend of an enterprise only when it reaches at the stage of commercial profitability. It is much less expensive and much more productive than commercial borrowings. The type of technology imported is likely to be up to date technology, accompanies by management expertise in manufacturing and quality culture, open up export markets, global contacts and outlets of the parent firm. In a nutshell, there is a global realization that it is much better to rely on foreign equity investment, rather than on external commercial loans, especially when major structural changes are being introduced in the economy[7].

FDI inflows in India

Normally FDI inflows in India are studied under three sub periods since Independence namely, FDI inflows during 1948-1980, during 1981-1990 and FDI inflows since 1991. The total FDI inflows from April 2000 to January, 2013 (in terms of Cumulative amount of FDI Equity inflows excluding amount remitted through RBIs NRIs schemes)works out to Rs.8,78,429 crores but for the Financial Year 2012-13 i.e., from April 2012 to January 2013, FDI equity inflows Rs.1,03,956 crores. For 2011-12 (up to January 2012) it works out to Rs.1,46,079 whereas for 2012-13 (up to January 2013), it amounted to Rs.1,03,956 crores. Actually, there is a decline to the extent of (-) 28 per cent[8].

Share of Investing Countries

Taking into account of 134[9] countries and FIIs, NRS and other countries , the details are awaited) the total of Rs.878428.70 the share of top 10 countries as a percentage to the total, Mauritius occupies with 38.08 per cent and UAE with 1.27 per cent. It can be concluded that FDI policy measures are more suitable to Mauritius than the other countries and that is the reason why nearly 38.08 per cent comes from that country alone.



Top 10 FDI Equity Inflows – Share of Investing Countries From April 2000 to January 2013

S.No.	Name of the Country	Amount of FDI inflows (in Rupees Crores)	Percentage with total FDI inflows
1	Mauritius	333979.10	38.08
2	Singapore	87555.85	9.99
3	UK	80285.89	9.22
4	Japan	67159.20	7.57
5	USA	50615.20	5.82
6	Netherlands	40543.75	4.54
7	Cyprus	32034.89	3.60
8	Germany	24031.97	2.74
9	France	16536.19	1.85
10	UAE	11260.42	1.27
	Total		

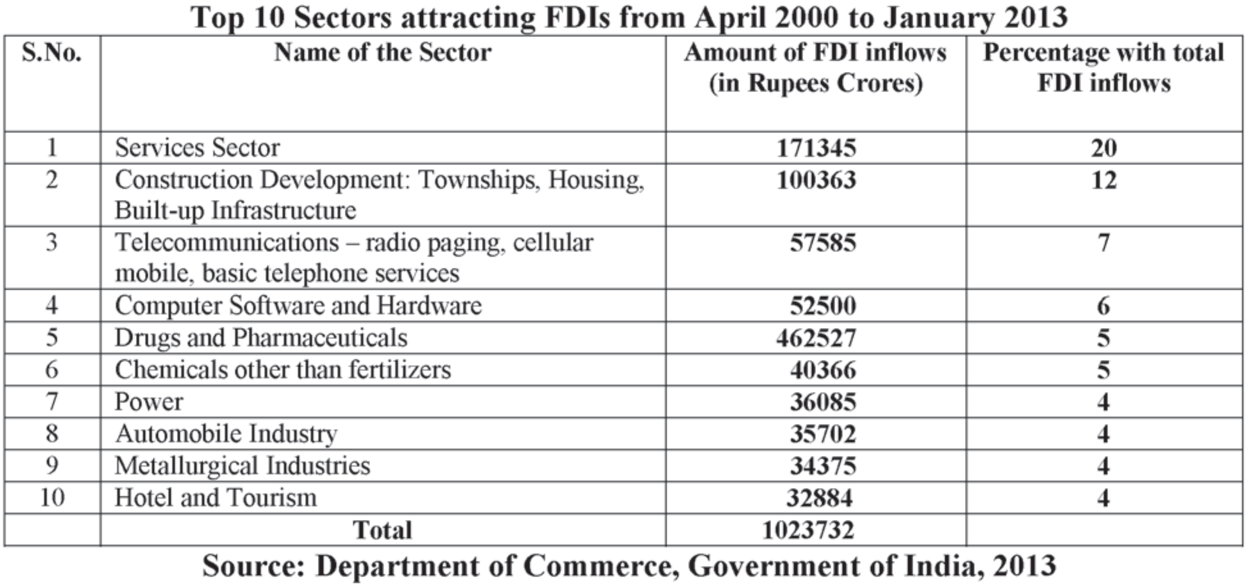
Source: Department of Commerce, Government of India, 2013

SECTORAL ANALYSIS

FDI inflows are welcomed currently in 63 sectors as compared to 16 sectors in 1991[10]. The sectors receiving the largest share of FDI inflows up to 2010 were the service sector and computer software and hardware sectors, each accounting for 22.14 per cent and 9.48 per cent respectively. Infrastructure sector received 28.62% of total FDI inflows from 1991-2008, Services sector received 19.34% of total FDI inflows from 1991-2008, Trading sector received 1.67% of total FDI inflows from 1991-2008, Consultancy Sector received 1.14% of total inflows from 2000-2008, Education sector received US $308.28 million of FDI inflows from 2004-2008, Housing and Real Estate Sector accounts for 5.78% of total FDI inflows during 2000-2008, Construction Activities Sector received 6.15% of the total inflows during 2000 to Dec. 2008, Automobile Industry received US $3.2 billion of total FDI inflows to the country during 2000 to 2008, Computer Software and Hardware sector received US $8.9 billion of total FDI inflows during 2000 to Dec.

2007 and Telecommunications Sector received an inflow of US $8.2 billion during 1991 to 2008.

Out of 63 Sector-Wise FDI Equity Inflows from April 2000 o January 2013[11], the following ten sectors plays a prominent role in the FDI inflows. The Financial, Banking, Insurance, Non-Financial/Business, Outsourcing, R&D, Courier, Testing and Analysis which falls under the Services Sector occupies the first place with 20 per cent, whereas construction development and telecommunications cornered 2nd and third positions respectively with 12 and 7 per cent.



Top 10 Sectors attracting FDIs from April 2000 to January 2013

S.No.	Name of the Sector	Amount of FDI inflows (in Rupees Crores)	Percentage with total FDI inflows
1	Services Sector	171345	20
2	Construction Development: Townships, Housing, Built-up Infrastructure	100363	12
3	Telecommunications – radio paging, cellular mobile, basic telephone services	57585	7
4	Computer Software and Hardware	52500	6
5	Drugs and Pharmaceuticals	462527	5
6	Chemicals other than fertilizers	40366	5
7	Power	36085	4
8	Automobile Industry	35702	4
9	Metallurgical Industries	34375	4
10	Hotel and Tourism	32884	4
	Total	1023732	

Source: Department of Commerce, Government of India, 2013

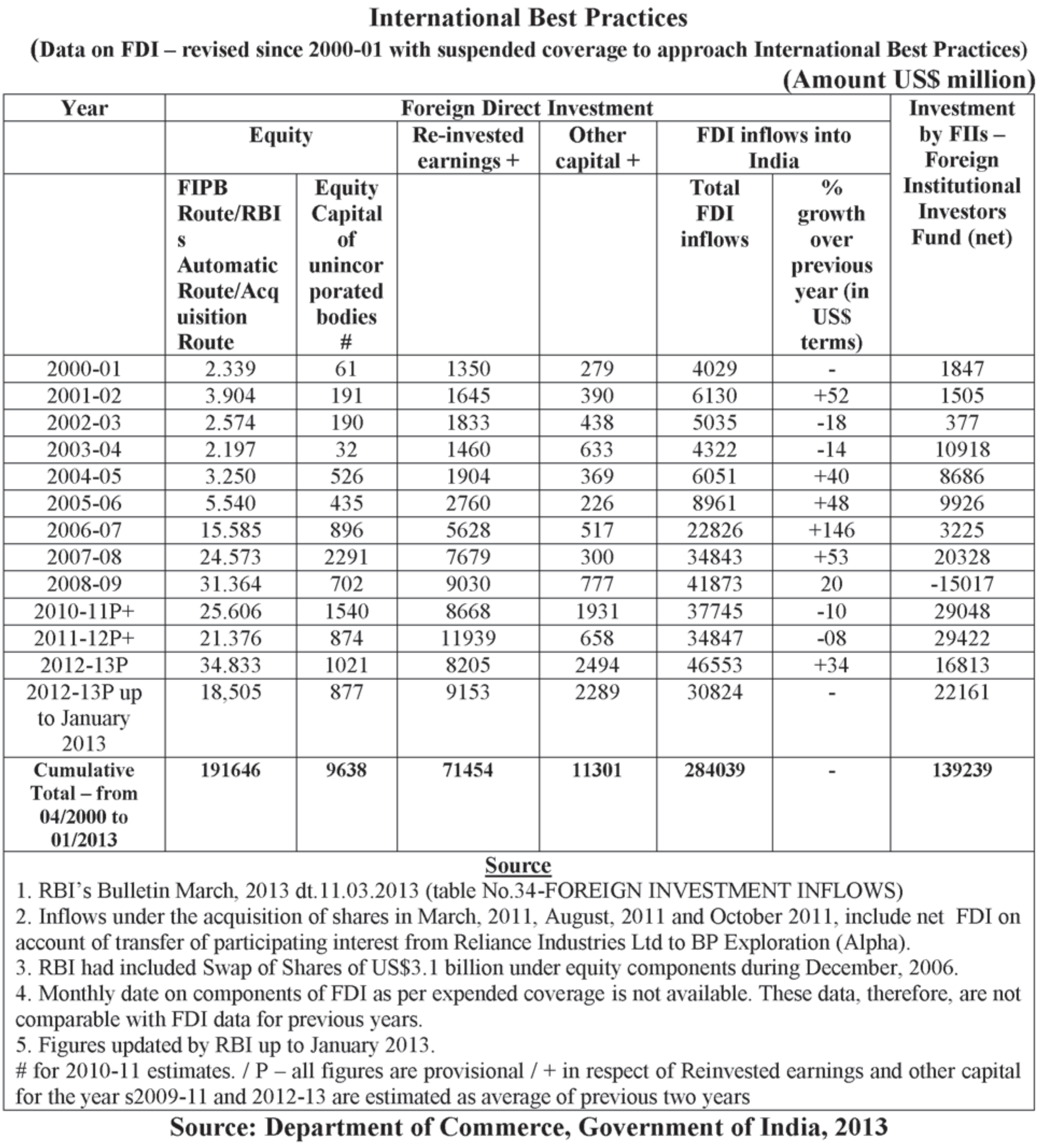
RBI's Regional Offices received FDI Equity inflows

Of the 16 RBI's regional offices, the first three positions are occupied by Mumbai, New Delhi and Bangalore with 33, 19 and 6 per cent respectively. In terms of US dollars it amounts to 62,144 for Mumbai Branch, 36,207 for New Delhi Branch and 10,561[12] for Bangalore branch. It can be concluded that Mumbai which happens to be the industrial base for India, it attracts more than any other branches in the country.

Reinvested earnings

The Government of India extended the definition of foreign direct investment (FDI) to include reinvested earnings by overseas investors and also their borrowing and lending transactions with their subsidiaries in the country. The aim of this reclassification is to provide a more authentic picture of FDI flows into the country and also to align these with the International Monetary Fund's definition of FDI. This is a mandatory requirement considering that India is also a subscriber to the IMF's Special Data Dissemination Standard (SDDS) established in 1996[13].

The IMF's definition of FDI includes equity capital, reinvested earnings and other direct investment capital. Equity capital covers equity in branches all shares in subsidiaries and associates (except non-participating preferred shares that are treated as debt securities) and other capital contributions. Reinvested earnings consist of the direct investors' share of earnings not distributed as dividends by subsidiaries or associates and earnings of branches not remitted to the direct investor. Taking this in to consideration, FDI data have been revised since 2000-01 with expended coverage to approach International Best Practices in US $ million which is a self explanatory from the following table.



International Best Practices

(Data on FDI – revised since 2000-01 with suspended coverage to approach International Best Practices)

(Amount US$ million)

Year	Foreign Direct Investment						Investment by FIIs – Foreign Institutional Investors Fund (net)
	Equity		Re-invested earnings +	Other capital +	FDI inflows into India		
	FIPB Route/RBIs Automatic Route/Acquisition Route	Equity Capital of unincorporated bodies #			Total FDI inflows	% growth over previous year (in US$ terms)	
2000-01	2.339	61	1350	279	4029	-	1847
2001-02	3.904	191	1645	390	6130	+52	1505
2002-03	2.574	190	1833	438	5035	-18	377
2003-04	2.197	32	1460	633	4322	-14	10918
2004-05	3.250	526	1904	369	6051	+40	8686
2005-06	5.540	435	2760	226	8961	+48	9926
2006-07	15.585	896	5628	517	22826	+146	3225
2007-08	24.573	2291	7679	300	34843	+53	20328
2008-09	31.364	702	9030	777	41873	20	-15017
2010-11P+	25.606	1540	8668	1931	37745	-10	29048
2011-12P+	21.376	874	11939	658	34847	-08	29422
2012-13P	34.833	1021	8205	2494	46553	+34	16813
2012-13P up to January 2013	18,505	877	9153	2289	30824	-	22161
Cumulative Total – from 04/2000 to 01/2013	**191646**	**9638**	**71454**	**11301**	**284039**	**-**	**139239**

Source

1. RBI's Bulletin March, 2013 dt.11.03.2013 (table No.34-FOREIGN INVESTMENT INFLOWS)
2. Inflows under the acquisition of shares in March, 2011, August, 2011 and October 2011, include net FDI on account of transfer of participating interest from Reliance Industries Ltd to BP Exploration (Alpha).
3. RBI had included Swap of Shares of US$3.1 billion under equity components during December, 2006.
4. Monthly date on components of FDI as per expended coverage is not available. These data, therefore, are not comparable with FDI data for previous years.
5. Figures updated by RBI up to January 2013.

for 2010-11 estimates. / P – all figures are provisional / + in respect of Reinvested earnings and other capital for the year s2009-11 and 2012-13 are estimated as average of previous two years

Source: Department of Commerce, Government of India, 2013

RECENT TREND

While addressing students and faculty on "The Rise of the East" Implications for the Global Economy by P. Chidambaram, Union Minister of Finance, Government of India, 16 April, 2013 at the South Asian Institute and Mahendra Humanities Center at Harvard University said that India has all the qualities to guarantee that foreign investment is protected and not affected by whims of governments. He also cited three things that requires for guaranteeing their capital i.e., "a stable and democratic political structure, a belief in the rule of law, and a transparent and independent legal system[14]".

The recent report by the Asian Development Bank's forecast a pick-up in economy activity in the first half of 2013 and forecast 8.2 per cent GDP growth for the full year will attract more FDI into the country[15]. Premier Lie[16] of China says that "China still faces a complex situation due to instability and uncertainty domestically and abroad. Wang Tao[17], Chief China Economist at UBS AG in Hong Kong says that as per the Bloomberg Survey there is a slowdown in light industrial production, weak consumption partly affected by a Government frugality campaign and export gains that are not as strong as customs figures. Zhu Haibin[18], Chief China Economist a JPMorgan

Chase and Co says that the story of China is “very disappointing slow recovery which is very weak in nature and bumpier than expected, dragged down by soft domestic demand. All these things will definitely go a long way in getting more FDI inflows into the country.

The trend in FDI at present is towards Insurance sector. Increasing FDI in the insurance sector is top priority for the present Government in power. It is the main subject in the present Parliament Session which opens on April 22, 2013[19]. Multinationals are managing to counter FDI restrictions and supply chain challenges at the most possible way showing path to others who are hesitant to enter into Indian market. For example Wal-Mart has taken steps to develop supply chains, procure 30-35 per cent local produce, making changes to its stock policy by reducing inventories. Auto majors are pumping money in the sector and Ford planned to invest US $500mn in its Chennai plant, Nissan-Renault planning to manufacture ultra-low-cost car with its local partner Bajaj Auto, French tyre maker Michelin’s to invest US$874mn in its first Indian manufacturing facility. All these developments are helping in getting FDI inflows into the country. As per the fact sheet on FDI, there was Rs 6,303.36 billion FDI equity inflows between the periods of August 1991 to January 2011.

CONCLUSION

Proposals for India’s biggest opening to FDI since the 1990s will be ready by June 2013 as the Government extends reforms to revive growth before the next general election. The economy is in need of more than $75 billion annually to finance the shortfall in its current account the broadest measure of trade. At present the gap swelled to $32.6 billion in the quarter ended 31st December, 2012 or 6.7 per cent of GDP, stirred up by gold and oil imports and unresponsive exports. The Finance Minister is under pressure to prevent a recurrence of the 1991 financial crisis, which prompted India to pledge gold as collateral for a loan from the International Monetary Fund after foreign exchange reserve slid. The present day current account deficit has led the nation to change policies since September, 2012 by easing curbs and levies on capital inflows. The benefits by way of FDI are of something great for the country.

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