# Role of Foreign Direct Investment in Indian Economy

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## Abstract

Foreign direct investment plays a very important role in the development of the nation. It is very much important in the case of underdeveloped and developing countries. In India FDI is considered as development tool and for foreign countries India is hot destination to investment. Foreign companies invest in India to advantage of relatively lower wages, special investment privileges such as Tax exemptions , etc. In India foreign investment was introduced in 1991 under Foreign Exchange Management Act FEMA , driven by then finance minister Manmohan singh .In this paper we study what are factors which influence the flow of FDI India and what are the problems relating to inflow of FDI.. Results of paper also find that Mauritius is the main provider of FDI to India . Nine of the 10 largest foreign business organization investing in India from April 2000 to January 2011. In fact 39.6% of FDI to India came from Mauritius between 2001 to 2011.

**Keywords**
Foreign Direct Investment , Factor influencing , Entry route, Finance

## Objectives

- To study why Mauritius is Main provider of FDI in India
- Determine the factor influencing FDI in India
- To identify the problems relating to inflow of FDI in India

## Methodology

The study is based on secondary data .The data collected from various published source such as Economic Survey government of India , various journals related to FDI, Websites of government, Books and Magazines related to FDI.

**Introduction**

FDI have helped India to attain a financial stability and economic growth with the help of investment in different sectors. FDI has boosted the economic life of India . Foreign direct investment help the economy generating employment to unemployed ,development of infrastructure , balanced economy ,less brain drain etc. After the liberalization trade policy become attractive due to this GDP of India is growing rapidly .In India FDI inflow made its entry during the year 1991-92 with the aim to bring together the intended investment and the actual saving of the country. To pursue a growth of around 7 % in GDP in India , the net capital flows increase by at least 28 to 30 % on the whole.

The concept of foreign Investment comes from the Foreign Exchange Management Act in 1991 driven by the finance minister Manmohan singh. Basically FDI is classified as inward FDI and outward FDI. Inward FDI means those foreign investments which are invested in local resources and outward FDI referred to as direct investment which is invested abroad.

In India there are two entry route of FDI:

**Automatic route:** By this route FDI is allowed without prior approval by government or RBI

**Government route:** Prior approval by government is needed via this route. Foreign investment promotion Board will be abolished in 2018 which was the responsible agency to oversee this route.

**REVIEW OF LITERATURE**

The vast literature on foreign direct investment and multinational corporations has been surveyed. . some literature about this study are presenting here as below:

Balasundaram Maniam and Amitiava chatterjee (1998) studied on the determinants of US foreign investment in India; tracing the growth of US FDI in India and the changing attitude of the Indian Government towards it as a part of the liberalization program.

Lipsey (2002) discovered the effect of inward FDI on the economic growth of host country. If the foreign firms at the expence of lower productivity in domestic firms achieve higher productivity ,there might be no implications for aggregate output or growth.

**Mauritius is Main provider of FDI in India**

The tax treaty between India and Mauritius was signed in 1982 in keeping with India’s strategic interests in the Indian ocean and India’s close cultural links with Mauritius. The treaty provides for a capital gains tax exception to a Mauritius resident on transfer of Indian securities.

It is interesting to note that Mauritius has been a key contributor to the foreign direct investment inflows in India in the past 15 years. The data published by the Ministry of commerce reveals that the cumulative inflow from April 2000 to December 2015 from Mauritius has been a whopping Rs 465,163crores. The country that is next in line is Singapore with a FDI inflow in the same period amounting to INR 238,352crores. While Mauritius accounts for 34% of the all FDI in the period, Singapore accounts for 16%.

Mauritius has regain the position as top source of foreign direct investment into India by pushing Singapore to the second slot in 2014-15. Mauritius accounted for about 29 % of the country total FDI inflow last fiscal . In 2013-14 ,Singapore had replaced Mauritius as the top source of FDI into India.

**Share of top investing countries FDI equity inflows (April 2015-June 2015) in crores**

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|---|---|
| **1** Singapore | **23,320 Rs** |
| **2** Mauritius | **13,236 Rs** |
| **3** Netherlands | **4,123 Rs** |
| **4** USA | **3,959 Rs** |
| **5** Germany | **3,497 Rs** |
| **6** Japan | **2,916 Rs** |
| **7** France | **877 Rs** |
| **8** UK | **755 Rs** |
| **9** Cyprus | **608 Rs** |
| **10** Switzerland | **598 Rs** |

**Total 60,298crore**
**Statement on RBI's**

**Factor influencing foreign direct investment in India**

**Wage rate**
A major incentive for a foreign companies to invest in abroad is lower wage rate. If average wages in the US $15 an hour, but $1 an hour in India , due to their cost is reduced. This is why many western firms have invested in clothing factories in the Indian sub-continent.

**Tax rates**
Big MNC , such as Apple, Google and Microsoft have sought to invest in countries with lower corporation tax rates.

**Infrastructure**
A key factor in the desirability of investment are the transport costs and level of infrastructure. A country may have low labour cost, but if there is then high transport costs to get the goods on to the world market, this is a drawback.

**Labour skills**
Some industries require higher skilled labour, for example pharmaceuticals and electronic. Therefore multinationals will invest in those countries with a combination of low wages, but high labour productivity and skills.

**Potential of growth**
FDI is often targeted to selling goods directly to the country involved in attracting the investment. Therefore , the size of population and scope for economic growth will be important for attracting investment.

**Political environment**
Countries where there is uncertainty about political situation ,will be a major disincentive. Related to political stability is the level of corruption and trust in institutions, especially judiciary and the extent of law and order

**Exchange rate**
A weak exchange rate in the host country can attract more FDI because it will be cheaper for the multinational to purchase assets . however ,,exchange rate volatility could discourage investment .

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**Problems relating to inflow of FDI in India**

**FDI opposed by local people**

- Domestic companies fear that they lose their ownership to overseas company
- Small enterprises fear that they may not be able to compete with world class companies and may ultimately be edged out of business.
- Large giants of the world try to create monopoly and take the highly profitable sectors
- Government has less control over the functioning of such companies as they usually work as wholly owned subsidiary of an overseas company.

**Resource challenge**

India is known to have huge amounts of resources. There is manpower and significant availability of fixed and working capital. At the same time , there are some underexploited or unexploited resources. The resources are well available in the rural as well as the urban areas. The focus is to increase infrastructure 10 years down line, for which the requirement will be an amount of about US $ 150 billion .

**Equity challenge**

India is definitely developing in a much faster pace now than before but in spite of that it can be identified that development have taken place unevenly. This means that while the more urban areas have been tapped , the poorer sections are inadequately exploited. To get the complete picture of growth , it is essential to make sure that the rural sections has more or less the same amount of development as the urbanized ones.

**Political challenge**

The support of the political structure has to be there towards the investing countries abroad. This can be worked out when foreign investors put forward their persuasion for increasing FDI capital in various sector like banking and insurance. So , there has to be a common ground between the parliament and the foreign countries investing in India. This would increase the reforms in the FDI are of the country.

**Federal challenge**

very important among the major challenges facing larger FDI , is the need to speed up the implementation of policies, rules, and regulations. The vital part is to keep the implementation of polices in all the states of India at par. Thus , asking for equal speed in policy implementation among the states in India is important

**Conclusion**

FDI in India has contributed effectively to the overall growth of the economy in the recent times. FDI policy permit FDI up to 100 % from foreign / NRI investor without prior approval in most of the sectors including the services sector under automatic route. India should use its advantages such as large domestic market , abundant supply of trained and low-wage labor , vast pool of technical professional, second largest nation, etc. Lack of proper infrastructure , instable government , high corporate tax rates and limited export processing zones are considered to the major problems for low FDI into the country. To overcome this situation , the government should revise the sectoral cap and bring more sectors under the automatic route. Further , India should sign the agreement of Double Taxation treaties with other countries in order to increase bilateral trade . therefore , there is an urgent need to adopt innovative policies and good corporate governance practices on par with international standards, bby the government of india. To attract more and more foreign capital in various sectors of the economy to make india a developed economy.

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