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Original Research Article

Indian Economy and Foreign Direct Investment: With Special Reference to 2012-13

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Abstract:
Foreign direct investment (FDI) is direct investment into production or business in a country by a Company in another country, either by buying a company in the target country or by expanding Operations of an existing business in that country. Foreign direct investment is in contrast to portfolio investment which is a passive investment in the securities of another country such as stocks and bonds.
FDI or Foreign Direct Investment, is Fund flow between the countries in the form of Inflow or Outflow by which one can able to gain some benefit from their investment, whereas another can Exploit the opportunity to enhance the productivity and find out better position through Performance. The potential advantages of the FDI on the host economy are it facilitates the use And exploitation of local raw materials; it introduces modern techniques of management and Marketing, it eases the access to new technologies.
Sources of Data: - This Research paper is totally based on Secondary data. All data are collected Through various web sites.

Key words: - FDI, Investment, Business.

Introduction:

Foreign direct investment (FDI) is direct investment into production or business in a country by a company in another country, either by buying a company in the target country or by expanding operations of an existing business in that country. Foreign direct investment is in contrast to portfolio investment which is a passive investment in the securities of another country such as stocks and bonds.

Foreign direct investment can take on many forms and so sometimes the term is used to refer to different kinds of investment activity. Commonly foreign direct investment includes "mergers and acquisitions, building new facilities, reinvesting profits earned from overseas operations and intercompany

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loans."However, foreign direct investment is often used to refer to just building new facilities or Greenfield investment, creating figures that although both labeled FDI, can't be side by side compared. **http://online.wsj.com**

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Foreign direct investment in India

Starting from a baseline of less than $1 billion in 1990, a recent UNCTAD survey projected India as the second most important FDI destination (after China) for transnational corporationsduring 2010–2012. As per the data, the sectors that attracted higher inflows were services, telecommunication, construction activities and computer software and hardware. Mauritius, Singapore, US and UK were among the leading sources of FDI. Based on UNCTAD data FDI flows were $10.4 billion, a drop of 43% from the first half of the last year. **http://online.wsj.com/article**

India disallowed overseas corporate bodies (OCB) to invest in India.

http://rbidocs.rbi.org.in/rdocs

2012 FDI Reforms

On 14 September 2012, Government of India allowed FDI in aviation up to 49%, in the broadcast sector up to 74%, in multi-brand retail up to 51% and in single-brand retail up to 100%.(**economictimes.indiatimes.com**)The choice of allowing FDI in multi-brand retail up to 51% has been left to each state.

In its supply chain sector, the government of India had already approved 100% FDI for developing cold chain. This allows non-Indians to now invest with full ownership in India's burgeoning demand for efficient food supply systems. (www.freshplaza.com)The need to reduce waste in fresh food and to feed the aspiring demand of India's fast developing population has made the cold supply chain a very exciting investment proposition.

Foreign investment was introduced by Prime Minister Manmohan Singh when he was finance minister (1991) by the government of India as FEMA (Foreign Exchange Management Act). This has been one of the top political problems for Singh's government, even in the current (2012) election. (http://timesofindia.indiatimes.com)(http://timesofindia.indiatimes.com)

FDI Policy Framework

Policy regime is one of the key factors driving investment flows to a country. Apart from underlying macro fundamentals, ability of a nation to attract foreign investment essentially depends upon its policy regime - whether it promotes or restrains the foreign investment flows. This section undertakes a review of India□s FDI policy framework and makes a comparison of India□s policy *vis-à-vis* that of select EMEs.

FDI Policy Framework in India

There has been a sea change in India’s approach to foreign investment from the early 1990s when it began structural economic reforms encompassing almost all the sectors of the economy.

Pre-Liberalization Period

Historically, India had followed an extremely cautious and selective approach while formulating FDI policy in view of the dominance of „import-substitution strategy□ of industrialization. With the objective of becoming „self reliant□, there was a dual nature of policy intention – FDI through foreign collaboration was welcomed in the areas of high technology and high priorities to build national capability and discouraged in low technology areas to protect and nurture domestic industries. The regulatory framework was consolidated through the enactment of

Foreign Exchange Regulation Act (FERA), 1973 wherein foreign equity holding in a joint venture was allowed only up to 40 per cent. Subsequently, various exemptions were extended to foreign companies engaged in export oriented businesses and high technology and high priority areas including allowing equity holdings of over 40 per cent. Moreover, drawing from successes of other country experiences in Asia, Government not only established special economic zones (SEZs) but also designed liberal policy and provided incentives for promoting FDI in these zones with a view to promote exports. As India continued to be highly protective, these measures did not add substantially to export competitiveness. Recognizing these limitations, partial liberalization in the trade and investment policy was introduced in the 1980s with the objective of enhancing export competitiveness, modernization and marketing of exports through Transnational Corporations (TNCs). The announcements of Industrial Policy (1980 and 1982) and Technology Policy (1983) provided for a liberal attitude towards foreign investments in terms of changes in policy directions. The policy was characterized by de-licensing of some of the industrial rules and promotion of Indian manufacturing exports as well as emphasizing on modernization of industries through liberalized imports of capital goods and technology. This was supported by trade liberalization measures in the form of tariff reduction and shifting of large number of items from import licensing to Open General Licensing (OGL).

Post-Liberalization Period

A major shift occurred when India embarked upon economic liberalization and reforms program in 1991 aiming to raise its growth potential and integrating with the world economy. Industrial policy reforms gradually removed restrictions on investment projects and business expansion on the one hand and allowed increased access to foreign technology and funding on the other. A series of measures that were directed towards liberalizing foreign investment included:

(i) Introduction of dual route of approval of FDI – RBIs automatic route and Government's approval (SIA/FIPB) route,

(ii) Automatic permission for technology agreements in high priority industries and removal of restriction of FDI in low technology areas as well as liberalization of technology imports,

(iii) permission to Non-resident Indians (NRIs) and Overseas Corporate Bodies (OCBs) to invest up to 100 per cent in high priorities sectors,

(iv) Hike in the foreign equity participation limits to 51 per cent for existing companies and liberalization of the use of foreign „brands name and (v) signing the Convention of Multilateral Investment Guarantee Agency (MIGA) for protection of foreign investments. These efforts were boosted by the enactment of Foreign Exchange Management Act (FEMA), 1999 [that replaced the Foreign Exchange Regulation Act (FERA), 1973] which was less stringent. This along with the sequential financial sector reforms paved way for greater capital account liberalization in India. Investment proposals falling under the automatic route and matters related to FEMA are dealt with by RBI, while the Government handles investment through approval route and issues that relate to FDI policy *per se* through its three institutions, *viz.*, the Foreign Investment Promotion Board (FIPB), the Secretariat for Industrial Assistance (SIA) and the Foreign Investment Implementation Authority.

FDI under the automatic route does not require any prior approval either by the Government or the Reserve Bank. The investors are only required to notify the concerned regional office of the RBI within 30 days of receipt of inward remittances and file the required documents with that office within 30 days of issuance of shares to foreign investors. Under the approval route, the proposals are considered in a time-

bound and transparent manner by the FIPB. Approvals of composite proposals involving foreign investment/ foreign technical collaboration are also granted on the recommendations of the FIPB. http://rbidocs.rbi.org.in

India FDI Inflows

The decade gone by would be considered as the golden year for foreign direct investment (FDI) in India. Between year 2000-11, India attracted cumulative FDI inflow of USD 237Bn. 70% of this FDI constituted equity inflows, rest being re-invested earnings and other capital. Over the last decade, FDI in India grew at CAGR 23% the Bull Run in India FDI started in FY 2006-07 when it grew at 146% over the previous year. FDI peaked in year FY2007-08 and only marginally declined in the following years of economic crisis. For the eight months of FY 2011- 12 (Apr- Nov 2011), India has already garnered USD 33 Bn. of FDI matching the full year FDI of the previous year. Share of top five investing countries in India stood at 69%. Mauritius was the top country of origin for FDI flows into India primarily driven by the tax haven status enjoyed by Mauritius. Services sector (Financial & Non-financial) attracted the largest FDI equity flows amounting SD 31 Bn. (20.5% share). Other high share sectors in top five were - Telecom (8%), Computer software & Hardware (7%), Housing & Real Estate (7%) and Construction (7%). Over the years, Automatic route has become the most used entry route for FDI investments in India indicating the gradual liberalization of FDI policy. In FY 2010-11, 64% of Equity FDI inflows in India came via “Automatic Route” almost trebling from 22% share in FY 2000-01. “Acquisition of shares” constituted 25% and “FIPB/SIA” constituted 11% of equity inflows in 2010-11.India’s FDI policy has progressively liberalized since nineties and only a few sectors, primarily in services sector.

Financial Sector FDI

Over the last decade, BFSI (Financial, Insurance & Banking services) was the most preferred destination for FDI in India. FDI in the BFSI sector accounted for over 12% of the total cumulative FDI inflows into India, and over 59% of the FDI in Services sector. Between 2000- 11, Services sector (BFSI and Non-Financial) attracted FDI of USD 31 Bn. With a 59% share, BFSI FDI share amounted to USD 18 Bn. The subsectors with BFSI attracted the following FDI equity inflows - Financial: USD 13 Bn., Banking: USD 2.9 Bn. and Insurance: USD 2.3 Bn. Mauritius had the largest share of FDI investment at 43% amongst top countries investing in Indian Financial services sector. Singapore (14%), UK (11%), USA (8.5%) and Cyprus (3%) were the other countries in the top five lists. Top 10 BFSI FDI Equity inflows in India over the last decade amounted USD 4.2 Bn. Key US investors in Indian BFSI sector included Merrill Lynch, Morgan Stanley, Bank of New York, Mellon, JP Morgan, Citibank Overseas, Franklin Templeton, New York Life, Metlife,AIG, Pramerica and PE/VC firms like Warburg, Blackstone, Carlyle, KKR & Co. and Apollo. Development of Indian capital markets (especially corporate bond markets) and further policy liberalization in commercial banking will be the key for future investments in Indian BFSI segment.

Foreign Direct Investment (FDI) in India in 2012-2013

'Indian economy is capable of absorbing US$ 50 billion in foreign direct investment (FDI) per year', said Mr. P Chidambaram, the Finance Minister, India. FDI is an economic segment that enjoys intense focus and attention from policy makers of the highest rank in the administration. The Government relaxed FDI regime in sectors including multi-brand retail, single-brand retail, commodity exchanges, power exchanges, broadcasting, non-banking financial institutions (NBFCs) and asset reconstruction companies (ARCs) in 2012.

There were several big-bang reforms and the Government allowed 51 per cent FDI in multibrand

Retail and 49 per cent in the aviation sector. FDI cap was also raised from 49 per cent to 74 per cent in broadcasting and ARCs, with an aim to bring foreign expertise in the segments. Foreign investment has also been allowed in power exchanges while foreign institutional investors (FIIs) have been allowed to invest up to 23 per cent in commodity exchanges without seeking prior approval from the Government. Thus, reforms and policies at such a massive level indicate that Indian FDI landscape offers a plethora of opportunities to foreign investors as the economy is booming and vibrant as compared to its global peers. Furthermore, favorable demographics and growth opportunities keep India an 'attractive' destination for merger and acquisition (M&A) activities across diverse sectors including consumer goods and pharmaceuticals, according to global consultancy Ernst & Young.

Key Statistics

India received FDI worth US$ 30.82 billion during April-January 2012-13 while FDI equity inflows during January 2013 stood at US$ 2.16 billion, according to latest data released by the Department of Industrial Policy and Promotion (DIPP). The sectors which have received high level of FDI during the first ten months of 2012-13 include services (US$ 4.66 billion), construction (US$ 1.21 billion), drugs & pharmaceuticals (US$ 1 billion), hotel and tourism (US$ 3.19 billion), metallurgical industries (US$ 1.38 billion) and automobile (US$ 895 million)

Country wise, high levels of FDI came during the period from Mauritius (US$ 8.17 billion), Singapore (US$ 1.82 billion), the UK (US$ 1.05 billion), Japan (US$ 1.69billion) and the Netherlands (US$ 1.52 billion), showed the DIPP data The value of M&A deals in India stood at US$ 4.5 billion in the March 2013 quarter, according to Thomson Reuters' India M&A First Quarter 2013 Review. Meanwhile, there were 90 private equity (PE) deals valuing US$ 1.04 billion during January-March 2013 quarter, reveal data from Four-S Services. India's foreign exchange (forex) reserves stood at US$ 292.64 billion for the week ended March 29, 2013, according to data released by the Central Bank. The value of foreign currency assets (FCA) - the biggest component of the forex reserves – stood at US$ 259.72 billion, according to the weekly statistical supplement released by the Reserve Bank of India (RBI).

Important Developments

The Indian Government, in consultation with the Foreign Investment Promotion Board (FIPB), has recently cleared 12 FDI proposals amounting to Rs 2, 609 crore (US$ 478.47 million). These included the proposal of Decathlon Sports India's proposal for infusion of foreign equity worth Rs 700 crore (US$ 128.37 million) to engage in single brand retail. The biggest proposal cleared was Ahmadabad-based Claris Otsuka Ltd's plan to accumulate its infusions in business into a new joint venture (JV) with FDI worth Rs 1,050 crore (US$ 192.56 million). The board also cleared Mumbai-based Glynwed Pipe System's proposal to receive foreign investment worth Rs 800 crore.

Other proposals to have received green signal included that of Promod S.A.S, France, to induct foreign equity worth Rs 29.69 crore (US$ 5.45 million) into an Indian JV company to be engaged in single brand retail trading and Fossil India and Le Creuset Trading's for setting up of single brand retail stores as a wholly-owned subsidiary (WoS) of a foreign company Japanese firm Mitsubishi has formed a JV with Dubai-based ETA Group to set up Mitsubishi Elevators ETA India Pvt Ltd, to manufacture, distribute, install and maintain elevators for premium residential apartment complexes and industrial buildings in India. The company, which was already present in India focusing on the premium commercial segment, will now focus on the premium residential segment and the middle segment in Tier 2 and Tier 3 cities. Meanwhile, French companies are showing keen interest to park

their investments in India, pertaining to segments like defense, space, urban development and infrastructure.

Policy Initiatives

The Indian Government is all-set to advertise in the world in the pursuit of reforms it has undertaken to woo foreign investments. While the Government is contemplating to raise FDI cap in defense sector to at least 49 per cent from the current 26 per cent, Mr. P Chidambaram has expressed confidence that the similar amendment could be introduced to the Insurance Bill very soon. The RBI will come out with a discussion paper by April 20, 2013 on redefining FDI and portfolio investment i.e. FII so as to remove ambiguities. The paper will have clarifications on legal and taxation issues involved in the implementation of the new definition, how the different

Instruments of foreign investments would be treated and how it would impact investments in listed and unlisted firms.

Also, the DIPP has released its latest edition of consolidated FDI policy which has incorporated in itself the changes made in the regulations over the past one year. The DIPP is the nodal agency on FDI related matters and with a view to make India's FDI regime simple and easy to understand for investors, it had compiled all the related policies into a single document.

Conclusion & Future Outlook

In the wake of several important announcements made by the Government over 2012-13, India is

Expected to receive higher FDI in 2013, said an official from the Commerce and Industry ministry. And believing that the trend would persist, HSBC has stated in its research report that there might be a shift in FDI flows from China to India in coming years. Exchange Rate Used: INR 1 = US$ 0.01834 as on April 11, 2013 http://www.ibef.org/india-at-aglance/foreign-direct-investment.aspx

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