Foreign Direct Investment (FDI) in India: Meaning, Policies and Challenges Ahead.

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INTRODUCTION

Foreign Direct Investment (FDI) is a process whereby residents of one country (the source country) acquire ownership for the purpose of controlling the management of an organization in another country (the host country). Individuals, as well as business entities, may undertake FDI.

Foreign Direct Investment (FDI) is a fund flow between the countries in the form of inflow or outflow by which one country 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 effectiveness and efficiency depends upon the investors' perception. If the investment is with the purpose of long term then it contributes positively towards economy, on the other hand if it is for short term, for the purpose of making profit then it may be less significant. Depending on the industry sector and type of business, a foreign direct investment may be an attractive and viable option. Any decision on investing is thus a combination of an assessment of internal resources, competitiveness, and market analysis and market expectations. The FDI may also affect due to the government trade barriers and policies for the foreign investments and leads to less or more effective towards contribution in economy as well as GDP of the economy.

Foreign direct investment (FDI) is when a company takes controlling ownership in a business entity in another country. With FDI, foreign companies are directly involved with day-to-day operations in the other country. This means they aren't just bringing money with them, but also knowledge, skills and technology.

With the initiation of globalization, developing countries, particularly those in Asia, have been witnessing an immense surge of FDI inflows during the past two decades. Even though India has been a latecomer to the FDI scene compared to other East Asian countries, its considerable market potential and a liberalized policy regime has sustained its attraction as a favourable destination for foreign investors.

Foreign direct investment (FDI) as a strategic component of investment is needed by India for achieving the economic reforms and maintains the pace of growth and development of the economy. The paces of FDI inflows in India initially were low due to regulatory policy framework but there is a sharp rise in investment flows from 2005 onwards because of the new policy has broadened.

Foreign Direct investment acts as a bridge to fulfil the gap between investment and saving. In the process of economic development foreign capital helps to cover the domestic saving constraint and provide access to the superior technology that promotes efficiency and productivity of the existing production capacity and generate new production opportunity.

When a firm controls (or have a strong say in) another firm located abroad, e.g. by owing more than 10% of its equity, the former is said "parent enterprise" (or "investor") and the latter "foreign affiliate". For a country, attracting an inflow of FDI strengthen the connection to world trade networks and thus finance its development path.

Background

The historical background of FDI in India can be traced back with the establishment of East India Company of Britain. After Second World War, Japanese companies entered Indian market and enhanced their trade with India, yet U.K. remained the most dominant investor in India. Further, after Independence issues relating to foreign capital, operations of MNCs, gained attention of the policy makers. Keeping in mind the national interests the policy makers designed the FDI policy which aims FDI as a medium for acquiring advanced technology and to mobilize foreign exchange resources. With time and as per economic and political regimes there have been changes in the FDI policy too. The industrial policy of 1965, allowed MNCs to venture through technical collaboration in India. Therefore, the government adopted a liberal attitude by allowing more frequent equity.

In order to boost the FDI inflows in the country Indian government allowed frequent equity participation to foreign enterprises apart from many incentives such as tax concessions, simplification of licensing procedures and de-reserving some industries like drugs, fertilizers, aluminium etc. But due to significant outflow of foreign reserve in the form of remittances of dividends, profits, royalties etc in 1973 Government of India set up Foreign Investment Board (FIB) and enacted Foreign Exchange Regulation Act (FERA) in order to regulate flow of FDI to India.

Further Government of India set up Foreign Investment Promotion Board (FIPB) for processing of FDI proposals in India. The Board is the apex inter-ministerial body of the Central Government that deals with proposals relating to FDI into India for projects or sectors that do not qualify for automatic approval by the Reserve Bank of India (RBI) or are outside the parameters of the existing FDI policy.

Types of Foreign Direct Investment

There are mainly two types of FDI- **Horizontal and Vertical.** However, two other types of FDI have emerged- **Conglomerate** and **Platform FDI.**

1. **HORIZONTAL FDI:** Under this type of FDI, a business expands its inland operation to another country. The business undertake the same activities but in foreign country.

2. **VERTICAL FDI:** In this case, a business expands into another country by moving to a different level of supply chain. Thus business undertakes different activities overseas but these activities are related to main business.

3. **CONGLOMERATE FDI:** Under this type of FDI, a business undertakes unrelated business activities in a foreign country. This type is uncommon as it involves the difficulty of penetrating a new country and an entirely new market.

4. **PLATFORM FDI:** Here, a business expands into another country but the output from the business is then exported to a third country.

Government initiatives

The Government of India has amended FDI policy to increase FDI inflow. In 2014, the government increased foreign investment upper limit from 26% to 49% in insurance sector. It also launched Make in India initiative in September 2014 under which FDI policy for 25 sectors was liberalised further.[13][14] As of April 2015, FDI inflow in India increased by 48% since the launch of "Make in India" initiative.[15] In May 2020, government increased FDI in defence manufacturing under the automatic route from 49% to 74%. In April 2020, government amended existing consolidated FDI policy for restricting opportunistic takeovers or acquisition of Indian companies from neighbouring nations.

India was ranked 15th in the world in 2013 in terms of FDI inflow, it rose up to 9th position in 2014 while in 2015 India became top destination for foreign direct investment. The Department for Promotion of Industry and Internal Trade and Invest India has developed the India Investment Grid (IIG) which provides a pan-India database of projects from Indian promoters for promoting and facilitating foreign investments.

Policy Initiatives

The Government of India has released a comprehensive FDI policy document effective from April 1, 2010. Furthermore, the government has allowed the Foreign Investment Promotion Board (FIPB), under the Ministry of Commerce and Industry, to clear FDI proposals of up to US$ 258.3 million. Earlier all project proposals that involved investment of above US$ 129.2 million were put up before the Cabinet Committee of Economic Affairs (CCEA) for approval. The relaxation would expedite FDI inflow.

The importance of FDI received special impetus towards the end of 1992 when the Foreign Institutional Investors (FIIs) such as pension funds, mutual funds, investment trusts, asset management companies, nominee companies and incorporated / institutional portfolio managers were permitted to invest directly in the Indian stock markets. In order to attract portfolio investments which prefer liquidity, it has been advocated to develop the Indian stock markets. The foreign portfolio investment not only do they expand the demand base of the stock market, but also stabilize the market through investor diversification.

In 2013, the government relaxed FDI norms in several sectors, including telecom, defence, PSU oil refineries, power exchanges and stock exchanges, among others. In retail, UK-based Tesco submitted its application to initially invest US$ 110 million to start a supermarket chain in collaboration with Tata Group's Trent. In civil aviation, Malaysia-based Air Asia and Singapore Airlines teamed up with Tata Group to launch two new airline services. Also, Abu Dhabi-based Etihad picked up a 24 per cent stake in Jet Airways that was worth over Rs 2, 000 crore (US$ 319.39 million). India has received total foreign investment of US$ 306.88 billion since 2000 with 94 per cent of the amount coming during the last nine years.

Foreign direct investment in India: FDI and Economic Growth

While India’s economy is largely agrarian, it has a booming services sector including construction, retail, software, IT, communications, hospitality, infrastructure operations, education, healthcare, banking and insurance, and many other economic activities. The services sector alone accounts for 55.6% of the total GDP. India has made a mark on the global economy with one of the world's fastest growing e-commerce markets.

Foreign investment plays a significant role in development of Indian economy. Many countries provide many incentives for attracting the foreign direct invesment (FDI). Need of

FDI depends on saving and investment rate in any country. Foreign Direct investment acts as a bridge to fulfil the gap between investment and saving. In the process of economic development foreign capital helps to cover the domestic saving constraint and provide access to the superior technology that promotes efficiency and productivity of the existing production capacity and generate new production opportunity.

India's core strengths are skilled manpower, developed financial system, sound regulatory regimes and the long history of private sector made it the prime destination for foreign direct investment FDI. India can attract far more FDI by creating world class infrastructure, creating conducive labour, Intellectual property right and land acquisition laws for business. A recent initiative of government has improved India's rank on ease of doing business. Gujarat has attracted more FDI than Chain's state is evidence of it.

China has attracted massive foreign direct investment by business-friendly environment and huge infrastructure in term of logistic, skilled manpower. China's approval mechanism is centralised and incentives are linked to exports. The policy has clear objectives and enjoys political support and commitment.

The country has the world's sixth-largest consumer market, making it an attractive investment destination. Government initiatives implemented over the years have successfully made India a hub of opportunities for foreign investors. Foreign direct investment guidelines have been revised and liberalized over the years to increase the ease of doing business in the country.

India is a major monetary source for economic development in India. Foreign companies invest directly in fast growing private Indian businesses to take benefits of cheaper wages and changing business environment of India. Economic liberalization started in India in wake of the 1991 economic crisis and since then FDI has steadily increased in India, which subsequently generated more than one crore (10 million) jobs. According to the Financial Times, in 2015 India overtook China and the United States as the top destination for the Foreign Direct Investment. In first half of the 2015, India attracted investment of $31 billion compared to $28 billion and $27 billion of China and the US respectively.

To boost India's manufacturing sector "Make in India" program has been launched by the Government of India. The government of India and government of Maharashtra have organised make in India week to attract foreign investors. Various state governments have organised similar investor summits in order to generate huge job opportunities under Make in India Programme government has a clear objective of 'Net Zero imports' by 2020.

To achieve this objective government has permitted 100% FDI under automatic route, announced various financial incentives (like withdrawn of Basic customs duty and special additional duties from imports of various components, Modified Special Incentive Package Scheme (M-SIPS) and created Electronic Development Fund (EDF). For promoting innovation & R&D government has taken initiative and set up many centres in premiere academic institutions in PPP mode with NASSCOM, Education and Research Network (ERNT) and others. To address skill development government has started new schemes like (Digital Saksharta Abhiyan (DISHA), Visvesvaraya Ph.D. scheme for Electronics & IT etc.). India BPO Promotion Scheme (IBPS) and various steps for ease of doing business have been announced.

Our administration model is guided by the experts and it is aimed to bring in financial stability in Indian economy through our interactive platform that connects investors with investment opportunities in the country as we are in association with foreign investors of more than 15 countries worldwide who are looking to invest in the Indian market.

Routes through which India gets FDI

Automatic route: The non-resident or Indian company does not require prior nod of the RBI or government of India for FDI.

Govt route: The government's approval is mandatory. The company will have to file an application through Foreign Investment Facilitation Portal, which facilitates single-window clearance. The application is then forwarded to the respective ministry, which will approve/reject the application in consultation with the Department for Promotion of Industry and Internal Trade (DPIIT), Ministry of Commerce. DPIIT will issue the Standard Operating Procedure (SOP) for processing of applications under the existing FDI policy.

FDI prohibition

There are a few industries where FDI is strictly prohibited under any route. These industries are:

- Atomic Energy Generation
- Any Gambling or Betting businesses
- Lotteries (online, private, government, etc)
- Investment in Chit Funds
- Nidhi Industry
- Agricultural or Plantation Activities (although there are many exceptions like horticulture, fisheries, tea plantations, Pisciculture, animal husbandry, etc)
- Housing and Real Estate (except townships, commercial projects, etc)
- Trading in TDR's
- Cigars, Cigarettes, or any related tobacco industry

FDI inflow

During the fiscal ended March 2019, India received the highest-ever FDI inflow of $64.37 billion. The FDI inflows were $45.14 billion during 2014-15 and $55.55 billion in the following year.

CONCLUSION

FDI always plays a role of a catalyst for the growth of the economic development by providing capital, transferring skills and technology and generating income & employment.
Make in India program is an initiative has started to boost manufacturing sector by improving infrastructure and business environment. India's rank on ease of doing business has been improved from last year by using single window concept. GST bill has been passed and the government is working aggressively to implement it. Skill India program is another step to generate skilled manpower for industry.
The prime minister himself visited around the world which has attracted huge Foreign Direct Investment in the country. India has caught up with China in FDI and this is bears testimony to the government's success and a step in the direction.
India's Foreign Direct Investment (FDI) policy has been gradually liberalised to make the market more investor friendly. The results have been encouraging. These days, the country is

consistently ranked among the top three global investment destinations by all international bodies, including the World Bank, according to a United Nations (UN) report. For Indian economy which has tremendous potential, FDI has had a positive impact. FDI inflow supplements domestic capital, as well as technology and skills of existing companies. It also helps to establish new companies. All of these contribute to economic growth of the Indian Economy.

Current Challenges and Improvement Areas

India is definitely a lucrative place for FDI, but there are certainly some challenges and areas for improvement still present. Until, these areas are honed to perfection, India will not become the number one place for FDI. India is focusing on maximizing political and social stability along with a regulatory environment. In spite of the obvious advantages of FDIs, there are quite a few challenges facing larger FDIs in India, such as:

- **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 the line, for which the requirement will be an amount of about US$ 150 billion. This is the first step to overcome challenges facing larger FDI.
- **Equity challenge:** India is definitely developing in a much faster pace now than before but in spite of that it can be identified that developments 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 section has more or less the same amount of development as the urbanized ones. Thus, fostering social equality and at the same time, a balanced economic growth.
- **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 sectors 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 area 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 policies in all the states of India at par. Thus, asking for equal speed in policy implementation among the states in India is important.
- India must also focus on areas of poverty reduction, trade liberalization, and banking and insurance liberalization. Challenges facing larger FDI are not just restricted to the ones mentioned above, because trade relations with foreign investors will always bring in new challenges in investments.

Last but not the least we can say without any hesitation, if things will move at this pace the day is not far when India will be one of the leading economies in the world.