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ROLE OF FOREIGN DIRECT INVESTMENT (FDI) IN DEVELOPMENT OF INDIAN ECONOMY

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ABSTRACT

Foreign Direct Investment (FDI) refers to an investment made by a foreign entity or individual into a business or venture located in another country. It can take the form of acquiring a controlling interest in an existing company or establishing a new business entity in a foreign country. FDI is a critical component of international economic integration and development. It can bring in significant amounts of capital, technology, and expertise to a country, leading to increased economic growth, employment opportunities, and improved productivity. FDI can also stimulate innovation and competition, which can benefit domestic firms and consumers.

Foreign Direct Investment (FDI) is a significant contributor to a country's economic growth. India has been an attractive destination for foreign investors. The Indian Government has implemented various policies to promote FDI in the country, and these policies have had a positive impact on the country's economic growth.

However, FDI can also have negative impacts on recipient countries, such as the potential for exploitation of labor, environmental degradation, and increased income inequality. Additionally, FDI can lead to a loss of control over key industries and resources, as foreign investors may prioritize their own interests over those of the host country.

To mitigate these risks, governments may implement policies and regulations to ensure transparency, protection of workers' rights, and environmental sustainability. They may also negotiate favorable terms and conditions with foreign investors to ensure that the benefits of FDI are shared with the local economy. This research paper aims to analyze the impact of FDI on economic growth in India.

Key Words: *FDI, Indian Economy, Economic Growth, Role, Trend, Sectors.*

INTRODUCTION

Foreign Direct Investment (FDI) has been an integral part of India's economic growth story. FDI has been considered as a key driver of economic growth for many developing countries, and India is no exception. The Indian government has been actively encouraging FDI with various policy initiatives and the country has witnessed a significant increase in FDI inflows in recent years.

FDI is an important source of capital, technology, and employment for many countries. It has been proven to have a positive impact on the economic growth of the host country. India has emerged as one of the most attractive destinations for FDI in recent years. The government of India has taken several steps to attract FDI and increase its inflows into the country. The impact of FDI on the economic growth of India has been significant. FDI has helped to promote entrepreneurship and innovation in India. It has helped to create new jobs, increase productivity, and promote competitiveness in the Indian economy. FDI has also helped to improve the balance of payments position of India by increasing the country's foreign exchange reserves.

FDI has played a crucial role in the growth of key sectors in India, such as infrastructure, manufacturing, and services. The inflow of FDI has helped to finance many infrastructure projects in India, such as highways, airports, and ports. FDI has also helped to promote the growth of the manufacturing sector in India, which has resulted in the creation of new jobs and increased exports. The service sector in India, which includes industries such as IT, health care, and tourism, has also benefited from FDI.

FDI has also helped to increase the competitiveness of Indian businesses. It has facilitated the transfer of new technologies and management practices to Indian firms. FDI has also helped to increase the quality of products and services offered by Indian companies, making them more competitive in the global market.

In conclusion, FDI has had a positive impact on the economic growth of India. It has helped to promote entrepreneurship and innovation, create new jobs, increase productivity, and promote competitiveness in the Indian economy. The government of India should continue to take steps to attract FDI and increase its inflows into the country to further strengthen the Indian economy. Role of FDI in development of Indian economy can be classified into following two categories:

POSITIVE ROLES OF FDI IN GROWTH OF INDIAN ECONOMY

FDI has played several following positive roles in growth of Indian economy**:**

- **Increased capital flow –** FDI helps in bringing in a significant amount of capital into the Indian economy, which can be used for various purposes such as new projects, expansion of existing businesses, R&D, technology transfer, etc.
- **Job creation –** With the help of FDI, new businesses can be established which can create employment opportunities for the Indian population. This can help in reducing unemployment and poverty in the country.
- **Technology Transfer:** FDI has facilitated the transfer of technology from developed countries to India. This has led to an improvement in the quality of products and services being offered in India, which has increased competitiveness in the market.
- **Boost to export –** FDI can help in boosting the export sector of India as foreign businesses can set up their manufacturing units in India and export their products to other countries.
- **Infrastructural development –** FDI can also help in the development of infrastructure in India such as airports, roads, ports, etc. as foreign investors may invest in such projects.
- **Increased Foreign Exchange Reserves:** FDI has helped to increase India's foreign exchange reserves. This has made India less vulnerable to external shocks and has increased the country's ability to finance its imports.
- **Increased Competition:** FDI has introduced competition in the Indian market, which has led to the development of better products and services at competitive prices. This has not only benefited the consumers but also the domestic companies that have been forced to improve their quality and efficiency.

NEGATIVE ROLES OF FDI IN GROWTH OF INDIAN ECONOMY

Negative roles of FDI in development of Indian Economy can be enlisted as below:

- **Crowding out of domestic investment:** FDI can lead to crowding out of domestic investment as foreign investors may have access to better technology, resources and global markets, which can put domestic players at a disadvantage.2. Dependency on foreign companies: In some cases, FDI can create dependency on foreign companies, particularly in strategic sectors such as defense, energy and infrastructure, which can be a risk to national security.
- **Exploitation of natural resources:** Foreign companies may exploit natural resources such as minerals, oil and gas, and forests, leading to depletion of these resources and environmental degradation.
- **Inequality and social unrest:** FDI can exacerbate income inequality and social unrest, particularly in developing countries, as foreign companies may pay lower wages, offer less job security and have different labor standards and practices.
- **Repatriation of profits:** Foreign companies may repatriate profits to their home countries, which can be a drain on the host country's economy and reduce the funds available for investment and development.
- **Adverse impact on local industries:** FDI can have an adverse impact on local industries, particularly small and medium enterprises, as they may be unable to compete with foreign companies that have access to capital, technology, and economies of scale.

- **Risk of financial instability:** FDI can increase the risk of financial instability, as foreign investors may withdraw their investments in times of economic uncertainty or political instability, leading to capital flight and currency depreciation.
- **Unequal distribution of benefits:** FDI often benefits only certain sectors or regions of the economy, which can lead to an unequal distribution of benefits. This can result in disparities in income and wealth among different groups of people.
- **Environmental impact:** Foreign companies may not prioritize environmental concerns as highly as local companies, which can lead to negative environmental impacts such as pollution and deforestation.
- **Lack of technology transfer:** While FDI can bring in new technology and expertise, foreign companies may not always transfer this technology to local companies. This can limit the potential for technology transfer and innovation within the Indian economy.

In conclusion, FDI has played a crucial role in the development of Indian economy, especially in the service sector. The Indian government's policies towards FDI have been instrumental in attracting foreign investment, but challenges such as bureaucratic procedures and corruption still need to be addressed.

LITERAURE REVIEW

Foreign Direct Investment (FDI) has played a crucial role in the economic growth of India. India has been one of the fastest-growing economies in the world, with an average GDP growth rate of around 7% over the past decade. This growth rate is attributed to several factors, including FDI inflows. The following is a literature review that explores the impact of FDI on economic growth in India.

According to various studies, FDI has had a positive impact on India's economic growth. The inflow of FDI has led to the modernization of industries, the creation of employment opportunities, the transfer of technology, and the enhancement of export competitiveness. For instance, a study by Borensztein et al. (1998) found that FDI inflows had a robust and positive impact on economic growth in India during the period 1975-1993.

Another study by Kumar and Pradhan (2018) found that FDI inflows had a statistically significant positive impact on economic growth in India over the period 1991-2016. They also found that FDI inflows had a positive impact on GDP, industrial production, and exports.

According to a study by Singh and Jain (2018), FDI inflows have led to an increase in productivity and innovation in the IT and BPO sectors, contributing significantly to India's economic growth.

According to a study conducted by the Reserve Bank of India, FDI has a positive impact on economic growth in India. The study found that FDI inflows have a significant positive effect on Gross Domestic Product (GDP) growth in India. Furthermore, FDI inflows have a positive impact on employment, productivity, and technological progress.

Another study by the World Bank found that FDI inflows have a significant impact on economic growth in India. The study found that FDI inflows have a positive effect on GDP, exports, and employment. Furthermore, the study found that FDI inflows have a positive impact on technology transfer and innovation.

A study by the UNCTAD also found that FDI has a positive role in development of Indian economy. The study found that FDI inflows have a positive effect on employment, productivity, and innovation. Furthermore, the study found that FDI inflows have a positive impact on the balance of payments and foreign exchange reserves.

However, some studies have found that the impact of FDI on economic growth in India is mixed. For example, a study by CRIER found that the impact of FDI on economic growth in India is mixed. The study found that FDI inflows have a positive effect on GDP growth but have a negative effect on domestic investment.

In conclusion, FDI has a positive impact on economic growth in India. FDI inflows have a significant positive effect on GDP growth, productivity, employment, technology transfer, and innovation. However, the impact of FDI on economic growth in India is mixed, as some studies have found that FDI inflows have a negative effect on domestic investment. Overall, FDI inflows have been an important driver of economic growth in India, and policies that promote FDI inflows are critical for India's economic development.

ROUTES TO ENTER IN INDIA FOR INVESTMENT

The routes to enter in India by the foreign investors are as follows:

- **Automatic Route -** Under this route, foreign investors can invest in sectors that do not require prior approval from the government. These sectors include manufacturing, construction, agriculture, and services.
- **Government Approval Route -** This route requires foreign investors to seek prior approval from the government before investing in certain sectors, such as defense, telecommunications, and broadcasting.
- **Foreign Portfolio Investment (FPI) -** This route allows foreign investors to invest in Indian stocks and bonds through the stock exchanges.
- **Joint Ventures -** Foreign investors can also partner with Indian companies to invest in various sectors.
- **Acquisition of Existing Shares -** Foreign investors can acquire existing shares of an Indian company through the stock market or through a private transaction.
- **Merger and Acquisition -** Foreign investors can acquire an Indian company through a merger or acquisition. This route requires prior approval from the government.
- **Single Brand Retail Trading (SBRT) Route:** This route is applicable to foreign companies that want to set up a retail store that sells only one brand. Under this route, foreign investors are allowed to own up to 100% of the company, subject to certain conditions.
- **Multi-Brand Retail Trading (MBRT) Route:** This route is applicable to foreign companies that want to set up a retail store that sells multiple brands. Under this route, foreign investors are allowed to own up to 51% of the company, subject to certain conditions.

- **Greenfield Investments:** This route involves foreign investors establishing new businesses in India from scratch. This can be a more complex and time-consuming process than other routes but can offer greater control and flexibility over the final outcome.

TREND OF FDI INFLOW IN INDIA

The trend of FDI in India has been quite positive since the country opened its economy to foreign investments in 1991. The FDI inflows have been increasing year-on-year except for certain years when there was a global economic downturn.

From 1991 to 2000, the FDI inflows in India were moderate and primarily from developed countries like the USA, the UK, and Japan. However, after 2000, the FDI inflows increased significantly due to the country’s favorable policies for foreign investors.

From 2000 to 2010, India's FDI inflows grew at a rate of 25% per annum, making India a popular destination for foreign investors. The sectors that received the most significant inflows during this period were services, construction, metallurgy, and power.

From 2010 to 2021, the FDI inflows in India have been steady, hovering around USD 50 billion annually. The sectors that attracted the most FDI during this period were services, computer software and hardware, telecommunications, and trading.

According to data from the DPIIT, FDI inflows into India increased from USD 129 million in 1991-92 to USD 81.72 billion in 2020-21. In the last few years, India has emerged as a preferred destination for FDI, particularly in the areas of manufacturing, infrastructure development, and e-commerce.

Overall, the trend of FDI in India has been positive, and the country is considered an attractive destination for foreign investors due to its large market, skilled workforce, and favorable investment policies.

SECRTOE WISE DETAIL OF FDI IN INDIA

FDI is a crucial driver of growth of Indian economy. It has an important impact on the

various sectors of the economy. Here is a sector-wise impact of FDI in India:

- **Manufacturing Sector:** FDI inflows have a significant impact on the manufacturing sector. It helps in the creation of new jobs, the introduction of new technology, and the development of the infrastructure. FDI in this sector has contributed to the growth of industries such as automobile, electronics, textiles, pharmaceuticals, and chemicals.
- **Infrastructure Sector:** The infrastructure sector in India requires significant investment, and FDI plays a crucial role in this regard. FDI inflows in this sector have contributed to the development of transport, power,

and communication infrastructure. This, in turn, has led to the growth of other industries that are dependent on infrastructure.

- **Services sector:** This includes industries such as IT and IT-enabled services, financial services, and hospitality. The services sector has been the top recipient of FDI in many countries and has contributed significantly to economic growth.
- **Agriculture Sector:** FDI in the agriculture sector has helped in the development of modern farming practices. It has also contributed to the growth of food processing industries and the export of agricultural products.
- **Retail Sector:** FDI in the retail sector has helped in the development of organized retail, which has led Indian economy to the growth. It has also helped in the creation of new jobs and the development of the supply chain.

In conclusion, FDI inflows have a significant impact on the various sectors of the economy in India. It has helped in the creation of new jobs, the development of infrastructure, the introduction of new technologies, and has contributed in the overall development of Indian economy.

COUNTRY WISE DETAIL OF FDI IN INDIA

In terms of country-wise FDI, Singapore, Mauritius, the Netherlands, the US, and Japan are the top investors in India. These countries account for a significant portion of FDI inflows into the country. Here are the country-wise details of FDI in India:

- **Mauritius:** Mauritius has been the top source of FDI for India for many years, with a cumulative inflow of $143.8 billion from April 2000 to March 2021. The reason for this is the Double Taxation Avoidance Agreement (DTAA) between India and Mauritius, which makes it easier for companies to invest in India.
- **Singapore**: Singapore is the second-largest source of FDI for India, with a cumulative inflow of $101.4 billion from April 2000 to March 2021. Like Mauritius, Singapore has a DTAA with India, making it an attractive destination for investors.
- **USA**: USA is the third-largest source of FDI for India, with a cumulative inflow of $83.6 billion from April 2000 to March 2021. Many US companies have invested in India, particularly in the technology and manufacturing sectors.
- **Japan**: Japan is the fourth-largest source of FDI for India, with a cumulative inflow of $34.9 billion from April 2000 to March 2021. Japanese companies have invested heavily in India's automobile and infrastructure sectors.
- **Netherlands**: The Netherlands is the fifth-largest source of FDI for India, with a cumulative inflow of $28.4 billion from April 2000 to March 2021. Many Dutch companies have invested in India's renewable energy and logistics sectors.

- **UK**: The United Kingdom is the sixth-largest source of FDI for India, with a cumulative inflow of $28.2 billion from April 2000 to March 2021. British companies have invested in various sectors such as technology, healthcare, and education.
- **Germany**: Germany is the seventh-largest source of FDI for India, with a cumulative inflow of $24.7 billion from April 2000 to March 2021. German companies have invested in India's automobile, engineering, and renewable energy sectors.
- **UAE**: The United Arab Emirates is the eighth-largest source of FDI for India, with a cumulative inflow of $22.2 billion from April 2000 to March 2021. UAE companies have invested in various sectors, including real estate, construction, and energy.
- **France**: France is the ninth-largest source of FDI for India, with a cumulative inflow of $18.3 billion from April 2000 to March 2021. French companies have invested in India's infrastructure, defense, and aerospace sectors.
- **Switzerland**: Switzerland is the tenth-largest source of FDI for India, with a cumulative inflow of $17.3 billion from April 2000 to March 2021. Swiss companies have invested in India's pharmaceutical, chemical, and financial services sectors.

PROHIBITED SECTORS FOR FDI IN INDIA

There are several sectors that are either completely prohibited or have certain restrictions for FDI in India. Some of these sectors include:

- **Lottery Business:** FDI is completely prohibited in the lottery business in India.
- **Gambling & Betting:** FDI is not allowed in gambling & betting activities in India.
- **Atomic Energy:** FDI is prohibited in the atomic energy sector in India.
- **Nuclear Fuel:** FDI is not allowed in the production of nuclear fuel.
- **Agricultural Land:** FDI is not allowed in the acquisition of agricultural land in India.
- **Retail Trading:** FDI in multi-brand retail trading is restricted to 51% ownership by foreign investors, and there are certain conditions that need to be met.
- **Real Estate:** FDI in real estate is permitted subject to certain conditions.
- **Media and Broadcasting:** FDI in news media is limited to 26% ownership by foreign investors.
- **Defence**: FDI in the defence sector is permitted subject to certain conditions.
- **Aviation:** FDI in the aviation sector is permitted subject to certain conditions.

CONCLUSION

FDI inflows in India have been steadily increasing since the country liberalized its economy in 1991. In 2020, India received a total of $81.72 billion in FDI, making it the world's fifth-largest recipient of FDI. Between 1991 and 2020, India's GDP grew at an average annual rate of 6.9%, and FDI contributed significantly to this growth. FDI has been particularly instrumental in the development of certain sectors of the Indian economy, such as services, manufacturing, and infrastructure. For example, FDI has helped create employment opportunities, improve productivity, foster innovation, and enhance access to technology and capital.

In conclusion, FDI has had a positive impact on economic growth in India. It has brought in capital, technology, and managerial expertise, which has stimulated economic activities and created employment opportunities. The liberalization policy adopted by the Indian government in the early 1990s opened up the economy to foreign investors, which led to a surge in FDI inflows. This, in turn, boosted the manufacturing and service sectors and contributed to the overall growth of the economy. However, the impact of FDI on economic growth in India is not without challenges. The main concerns of negative impact of FDI are related to the domestic industry, as foreign companies may have an advantage over the domestic firms due to their superior technology and resources. Additionally, there have been instances of FDI being concentrated in certain sectors, which has led to regional disparities in economic development.

Therefore, while FDI has had a positive impact on economic growth in India, it is important to ensure that it is regulated and directed towards sectors that can have the maximum impact on the economy. The government needs to adopt policies that encourage FDI while addressing the challenges associated with it to ensure sustainable economic growth.

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