



THE IMPACT OF FOREIGN INVESTMENT ON INDIA ECONOMY

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Abstract-If economy is a body, Investment is its blood and sometime body needs adequate blood for being healthy, we have to bring it from other body, means if an economy need to run with well health, investment is necessary for it and has to bring from other countries, which is called Foreign Investment. In the era of globalization and financial integration, Foreign Investment has emerged as one of the most important forms of capital flows to developing countries. The main objective of present study is to see the impact of Foreign Investment on Indian economy. The study is based on the period of 1991-92 to 2017-18. To analysis the data line graph, correlation and Regression with Newey-West standard errors are used. To check problem of unit root Interpolated Dickey-Fuller test has been also used. Evidences are collected from Reserve Bank of India: handbook of statistics on Indian Economy. In the result we found that there is positive impact on Indian economy and other variable such as Total Debt, Foreign Exchange Reserve, India's Foreign Trade are playing statistically significant positive role to improve economy except NRI's Deposits which impact is not statistically significant. Although, in the analysis, the result is also found that in the one hand; economy, Total Debt, Foreign Exchange Reserve and NRI Deposits are positive correlated but in the other hand; India's foreign trade is negatively with other variables. In the conclusion, foreign investment is not only an option of domestic investment, but can also improve the balance of payment of host country. The flow of foreign investment in an economy benefits the economy in terms of investment capital, technology transfer, management skills and job creation. At present, many developing and at least developed countries depend on foreign investment inflows due to less domestic investment and lack of resources.

Keywords: Foreign Exchange Reserve, Foreign Investment Inflows, India's Foreign Trade, NRI Deposits, Statistically Significant and Total Debt.

1. INTRODUCTION

Foreign Investment has been taking place in an increasingly liberalized framework. Government has been taking action to stimulated Foreign Investment and in many cases they have gone beyond creating a more liberal environment to provide substantial public subvention to attract Foreign Investment. Why Foreign Investment is so important? It is motivated by an assumption that the presences of foreign firms yield benefits in various ways, including higher economic development than other.

Economic integration and increasing movement of capital on international borders has dramatically changed the sources of local industrial development. Because firms have sought rehabilitation opportunities in areas around the world, so looking for new resources, cheap skills and new markets, governments around the world are ready for these investments. They are trying to use them as tools for development: to generate more employment, to promote exports, etc. And upgrade local skills and technical capabilities. How successful they are to achieve these developmental goals. A major question that comes out, which is from the perspective of the host countries trying to capture the developmental benefits of globalization: What are the circumstances under which to achieve the benefits of foreign investment in the areas of improvement Regional competitiveness, employment and development can be successful in this, and in this process some areas and countries are better than others. Thus do? What is the lesson of this public policy for governments that manage the effect of liberalization and internationalization on their regional industries?

2. REVIEW OF LITERATURE

Because of the importance of Foreign Investment, there have been substantial studies on this issue, both empirically and theoretically. Theoretically such as Froot, K.A., and Stein, J.C. (1991), Lipsey, R.E. (2002), Kojima, K., and Ozawa, T. (1984), Dunnin, J. H. (1988), Vernon, R. (1966), Nocke, V. and Yeaple, S. (2004). And empirically, Tiwari A K and Mutascu M (2011) examine the impact of foreign direct investment on economic growth in 23 Asian countries in their study; the period of study is 1986 to 2008. They find that foreign investment and exports enhance the growth of Asian countries and also that labour and capital help in that process. This implies that Asian countries that are moving ahead for globalization may choose to go ahead. They analyzed the case of nonlinearity associated only with foreign investment, and found that this variable enhances growth. On the other hand, the investigation of the nonlinearity in both cases shows a significant and positive impact of exports only on the economic growth of panel countries. Further, there are studies that have found that foreign investment has a negative impact on economic growth and income distribution.

Zakariya M and Shakoor M(2013), in their study, examine the impact of trade openness on foreign direct investment

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(foreign investment) in Pakistan using quarterly data for the period 1972 to 2010. They find that human and physical capitals, capital returns, infrastructure development, terms of trade and urbanization promote foreign investment in Pakistan. Macroeconomic instability (proxies by inflation rate) affects foreign investment negatively, and being highly indebted is a significant deterrent to foreign investment. Another important finding is that the effect of trade openness on foreign investment has been augmented after the inception of flexible exchange rate system in Pakistan. Mehrara M and Musai M (2015), find that there is a long-run relationship between foreign investment and GDP. Utilizing Granger Causality within the framework of a panel co-integration model, there is strong causality running from GDP to foreign investment with no feedback effects from foreign investment to GDP MENA region countries.

Archana Vani, Nayak N C & Basu P (2014), find that the overall impact of foreign investment on productivity and employment is quite encouraging for the period considered. They also find that across regions the impact is quite uneven. Those states where the labour productivity is raising due to foreign investment inflows generally revealed a significantly negative impact on employment except for Karnataka and Haryana, where the impact of foreign investment on both labour productivity and employment are positive and significant. The impact of foreign investment on labour productivity is negative in less developed states, while it has significant and positive effect in catching-up and more developed states where technology intensive sectors are predominantly prevailing.

3. OBJECTIVES

- i. To examine the trend and pattern of Foreign Investment in India
- ii. To analyse the relationship among Foreign Investment, per capita national income, Foreign exchange reserve, NRI deposits, foreign trade and total debt in India
- iii. To evaluate the impact of Foreign Investment with foreign exchange reserve, NRI deposits and total debt on economy of India.

4. METHODOLOGY

The present study is based on the period of study is 1991-92 to 2017-18, and also based on secondary evidences which are taken from various Reserve Bank of India hand book of Statistics on Indian Economy and World Bank Data. To analysis the data; line graph, correlation and Regression with OLS estimator are used. To check problem of unit root Interpolated Dickey-Fuller test has been also used. As an indicator of Economic Growth Per Capita National Income (PCNI) is used because PCNI is better indicator to examine the impact of Foreign Investment than Gross Domestic Product.

Hypothesis

H₀: There is no significant impact of Foreign Investment on Indian Economy

The model

$$PCNI = \alpha + \beta_1 \text{NRI Deposits} + \beta_2 \text{TD} + \beta_3 \text{FER} + \beta_4 \text{IFT} + \mu_i$$

5. RESULT AND ANALYSIS

The inflow of Foreign Investment in India changed the economy, it can be seen but relationship among Per capita national income (PCNI), NRI deposits, Total Debt (TD), Foreign Investment inflows (FII), Indian Foreign Trade (IFT), Foreign Exchange Reserve (FER) is seems in fig.5.1.

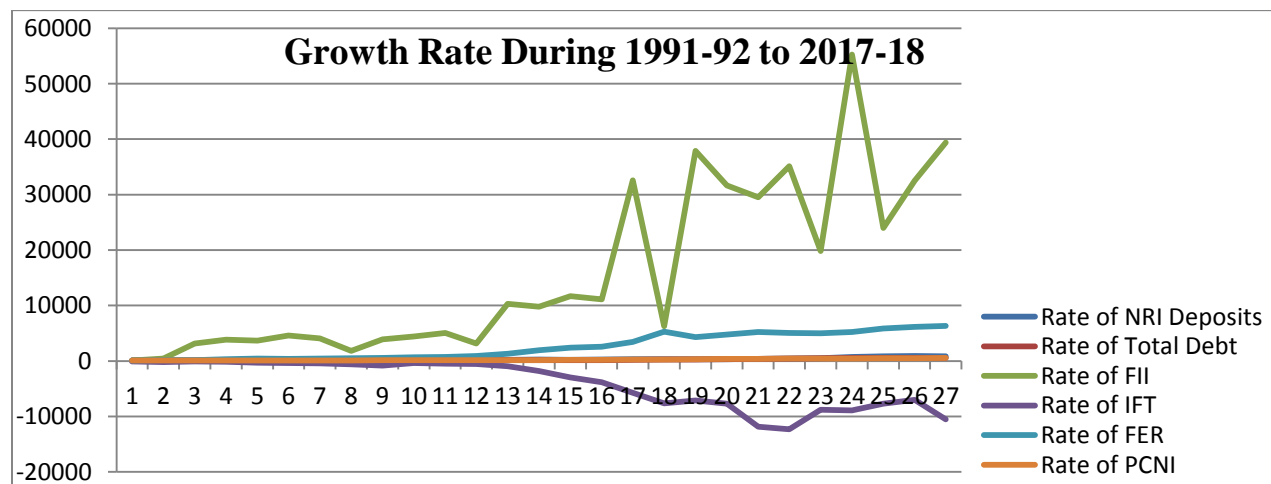


Fig. 5.1 Relationship among Different Growth Rates

Source: RBI hand book of statistics of Indian economy and data.worldbank.org

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The Table 5.1 is showing the path of growth rate of PCNI, NRI Deposits, TD, FII, IFT, and FER in the period of 1991-92 to 2017-18. It is seen in the table-1.1 that except the period of global depreciation (2007-08 to 2011-12) FII is increasing very much faster. And growth rate of IFT is negative due to higher import than export. But growth Rate of PCNI, TD, NRI Deposits is increasing slower but rate of FER is increasing more than others except FII. In the next Table-5.1, it can be seen the correlation among the PCNI, NRI Deposits, TD, FER, FII and IFT.

Table-5.1 Correlation among Different Growth Rates with PCNI

Correlation among PCNI, NRI Deposits, TD, FER, FII, IFT						Observation=27
Correlation	Per Cap NI	NRI Deposits	Total Debt	FER	FI Inflows	IFT
Per Cap NI	1.0000					
NRI Deposits	0.9216	1.0000				
Total Debt	0.9754	0.9615	1.0000			
Foreign Exchange Reserve	0.9750	0.8705	0.9233	1.0000		
Foreign Investment Inflows	0.8701	0.7754	0.8171	0.8376	1.0000	
India's Foreign Trade	-0.9399	-0.7496	-0.8688	-0.9474	-0.8461	1.0000

Source: RBI hand book of statistics of Indian economy and data.worldbank.org

since 1991-92, PCNI, NRI Deposits, TD, FER, FII are highly positive correlated with each other but IFT is correlated with others with very high degree of correlation because India is much dependent on other countries for his demand such as petroleum, Fertilizes and electronic materials, which make its' growth negative.

To examine the impact of Foreign Investment, it is needed to check problem of unit root in the time series data. As table-5.2 is showing that:

Table-5.2 Unit Root Test for Stationarity

Interpolated Dickey-Fuller test for unit root		Number of observations = 26
Variables	Test Statistic	5% Critical Value
NRI Deposits	3.097	-1.950
Total Debt	4.461	-1.950
Foreign Exchange Reserve	1.980	-1.950
Foreign Investment Inflows	-1.150	-1.950
India's Foreign Trade	0.657	-1.950

Source: calculated by statistical software

To check the problem of unit root, Interpolated Dickey-Fuller test individually with all factors at the 5% of level of statistical significance. After the test it is found that NRI Deposits, TD, FER do not have problem of unit root but FII and IFT do have the problem of unit root at the 5% level of significance.

To remove the problem of unit root from FII and IFT, both should be differentiated with first order. As table-5.3 shows:

Table-5.3 Unit Root Test for Stationarity with Fist Difference

Interpolated Dickey-Fuller test for unit root		Number of observations =26
Variable with first difference	Test Statistic	5% Critical Value
Foreign Investment Inflows	-12.440	-1.950
International Foreign Trade	-3.693	-1.950

Source: calculated by statistical software

After first order differentiation, FII and IFT are free from the problem of unit root statistically significant at 5% level of significance, to detect the problem of unit root same test (Interpolated Dickey-Fuller test) is applied individually. To analyzing the impact of FII on Indian economy, the regression is applied with OLS Estimator. The model is statistically significant at 1% of level of significance. PCNI is taken as indicator of Indian economy. The hypothesis is for the model: there is no impact of independent factors on Indian Economy.

Table-5.4 Regression Analysis with OLS Estimators

Regression Analysis				Number of Observations
				26
Source	Sum of squares	Degree of freedom	Mean of squares	F (5,20) 516.74
Model	6465596.69	5	1293119.34	Probability>F 0.0000
Residual	50049.4617	20	2502.47308	R² 0.9923
Total	6515646.15	25	260625.846	Adj R² 0.9904

Source: calculated by statistical software

Table-5.5 Significance of Variables

PCNI	Coefficients	Standard Error	t	P> t
Constants	166.1024	18.91388	8.78	0.000*
NRI Deposits	-0.0020322	0.0010884	-1.87	0.077***
TD	0.0023655	0.0003545	6.67	0.000*
FER	0.0018062	0.000229	7.89	0.000*
FII	0.0014557	0.0005521	2.64	0.016**
IFT	-0.0003316	0.0005303	-0.63	0.539 [#]

*statistically significant at 1% level of significance
 **statistically significant at 5% level of significance
 ***statistically significant at 10% level of significance
 #statistically not significant

Source: calculated by statistical software

The model

$$\text{PCNI} = 166.1024 - 0.0020322 \text{ NRI Deposits} + 0.0023655 \text{ TD} + 0.0018062 \text{ FER} + 0.0014557 \text{ FII} - 0.0003316 \text{ IFT} + \mu_i$$

The above model (by table-5.4 and table-5.5) is statistically significant at 1% of level of significance. R² is 0.9923 and adj R² is 0.9904 which means independent variables are explaining 99% of variation in dependent variable. PCNI is dependent on NRI Deposits, TD, FER, FII and IFT. Where FII and IF are used as first different variable. In the model, TD, FER and Constant coefficient are statistically significant at 1% of level of significance. FII and NRI Deposits are statistically significant respectively at 5% and 10% level of significance. And IFT is not statistically significantly.

The hypothesis is rejected at 5% of p-value; means there is a statistically significant impact on PCNI of FII.

It is showing in the model that if 1000 US \$ decrease in NRI Deposits, it will increase 2.0322 US \$ in PCNI. If 1000US \$ increase in Total Debt of India, will increase 2.3655 UD \$ in PCNI. If 1000 US \$ increase in FER, will increase 1.8062 US \$ in PCNI. And 1000 US \$ increase in FII will increase 1.4557 US \$ in PCNI.

CONCLUSION

However, a very confident development has given a tremendous boost to the recent budget which has given India industrial infrastructure and foreign investment. The positive side of the story is the tremendous flexibility of the economy, rapid development of Indian agriculture, increasing infrastructure, India has tremendous global outsourcing boom and a well-regulated and deep capital market. The flow of foreign investment in an economy benefits the economy in terms of investment capital, technology transfer, management skills and job creation. At present, many developing and at least developed countries depend on foreign investment inflows due to domestic investment and lack of resources. Foreign investment is not only an option of domestic investment, but can also improve the balance of payment of host country. It is one of the major stimuli for economic development of developing countries. In such a scenario, foreign investment plays an important role in generating jobs in the economic development and globalized world.

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