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Foreign Direct Investment Policy in India - A Study

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Abstract

FDI plays a crucial role in the country's growth and development. When a nation encounters a lack of capital for its overall development, foreign investment is the solution to bridge the gaps between domestic capital and investment. India has become a major global center for FDI, ranking among the top ten FDI destinations, as highlighted in the World Investment Report 2023. The nation has made significant progress in attracting foreign investments through major reductions in corporate taxes and the streamlining of labor regulations. Additionally, FDI serves as a key conduit for technology transfer, connecting advanced economies with developing countries. This transfer is not just a simple exchange of equipment and machinery; it represents the sharing of knowledge, innovative methods, and organizational capabilities that can significantly alter the productivity landscape of the receiving nation. The processes through which technology transfer takes place are complex and often interconnected, incorporating both direct and indirect pathways observable at the firm and industry levels. The current study aims to examine the sectorwise FDI limits in India.

Key words: *FDI, Capital, Investment*

1. Introduction

Foreign Direct Investment (FDI) is among the crucial key elements contributing to the economic development of a nation. FDI indicates an investment made by a business or individual in one country in the commercial interests of another country. This usually entails setting up business operations, purchasing assets, or expanding current facilities. FDI is an essential aspect of global economic integration and significantly impacts international trade

In India, FDI has surfaced as an important catalyst for economic growth and advancement. Following its economic liberalization in the early 1990s, India has proactively promoted FDI as a strategy to enhance capital inflow, improve technology transfer, and generate employment opportunities. During the pre-liberalization period, FDI was subject to stringent regulations, characterized by severe controls and a minimal foreign presence within the Indian economy. Post-economic liberalization, FDI in India witnessed the opening of its economy and the relaxation of restrictions on foreign investments. Furthermore, the government implemented reforms that permitted foreign companies to invest in various sectors under specific conditions. In 2000, FDI inflows rose due to the continuous easing of regulations and the promotion of investments through initiatives such as the Foreign Investment Promotion Board (FIPB)

FDI serves as a crucial engine of India's economic development, acting as a major non-debt financial resource for progress. Global corporations are increasingly putting their money into India, lured by unique incentives including tax advantages and competitive labor expenses. This influx of investment not only brings technological knowledge but also creates jobs and other secondary benefits. The increase in FDI can largely be attributed to the government's dynamic policy framework, a lively business climate, and India's rising influence in the global economy.However, some sectors are entirely prohibited from accepting FDI. Within the categories where FDI is permitted, there are still some sectors that impose restrictions on the proportion of foreign investment permitted. It is crucial for investors and companies looking for prospects in foreign markets to comprehend these restrictions

To strengthen FDI, the Indian government has initiated several programs, including the "Make in India" campaign, which seeks to streamline processes and foster an inviting investment environment. Major liberalizations in FDI regulations, particularly in areas such as retail, defense, and insurance, have been crucial. Moreover, the introduction of the Goods and Services Tax (GST) has improved transparency, while Special Economic Zones (SEZs) provide targeted tax incentives

Substantial investments in technology and healthcare have fostered strategic collaborations between multinational corporations (MNCs) and local companies, resulting in an extraordinary 83% rise in cross-border mergers and acquisitions (M&A) to US$27 billion in 2020. Based on the World Investment Report 2023, India has established itself as an FDI powerhouse, ranking third regarding investments in greenfield projects. From April 2014 to June 2024, India drew in a cumulative total of US$ 725.96 billion in FDI from 170 countries, covering 33 states and union territories across 63 sectors.

2. Review of Literature

For the study purpose some articles are studied and reviewed as follows.

N Prasanna'sresearch investigates the connection between FDI inflows and manufactured exports in India. It emphasizes the transition from primary commodities to higher value-added exports, as well as FDI's role in this shift. The research uncovers a positive relationship between FDI inflows and manufactured exports, indicating that domestic strategies should align with FDI policies for continued export growth.

Ravi Aluvala's research explores the changing dynamics of foreign direct investment (FDI) in India. It underscores differing perspectives on FDI and emphasizes the need to assess its costs and benefits. FDI is regarded as a possible catalyst for economic expansion, with liberalization policies being crucial in drawing FDI inflows. The research also addresses global competition for FDI and the increase of in India" offers an in-depth examination of FDI's role in India's development, concentrating on closing the saving-investment gap. It analyzes FDI pathways. The new FDI policy and Government initiatives to enhance FDI. Utilizing secondary data and analytical tools, the research classifies FDI pathways, reviews policy regulations, and pinpoints sectors with significant FDI potential. It anticipates a rise in FDI inflows owing to advantageous government policies

Sonia Chawla et.al, examined the dynamics of foreign investment in India following the 1991 liberalization. It points out the preeminence of the services sector in drawing foreign direct investment and foreign institutional investment. The study offers insightful perspectives on the factors influencing foreign investment flows in India, assisting policymakers in attracting and maintaining foreign investments.

Rudresha's analysis titled "Foreign direct investment in India" delivers a comprehensive examination of FDI's importance to India's development, with a focus on bridging the saving-investment gap. It investigates FDI routes. The new FDI policy, and government actions to enhance FDI. By applying secondary data and statistical methods, the analysis categorizes FDI pathways, discusses policy regulations, and identifies sectors with strong FDI potential. It forecasts augmented FDI inflows due to supportive government policies.

3. Objectives of the Study

The primary objective of the present study to study a bird eye view of FDI inflow in India and other secondary objectives of the paper are presented below.

1. To understand the sector-wise FDI limits in India.
2. To Analyse the role of FDI in facilitating technology transfer in India.
3. To study the sector-wise and year-wise analysis of FDI in India.
4. To know the country-wise flow of FDI in India.
5. To highlight the Government measures to increase FDI in India

4. Research Methodology

The research paper is a descriptive in nature. The study was done only through the secondary data. The secondary data collected from various published and unpublished sources like Reserve Bank of India (RBI) United Nations Conference for Trade and Development (UNCTAD), Ministry of Commerce and Industry, economical survey report and journal etc. And also some statistical tools used to analyze the data.

Restricted Sectors

These are areas where Foreign Direct Investment (FDI) is entirely forbidden. The restriction may arise from several factors, including national security, cultural preservation, or public health. Below is the full list of Prohibited Sectors in India.

- **Permitted Sectors with 100% FDI:** In certain sectors, foreign investors are allowed to set up a company in India with 100% equity without needing any previous government approval; however, a notification upon receiving the FDI remittance is to be submitted to the RBI in the form of FC-GPR. This policy exists to promote foreign investment in sectors vital for economic progress, like information technology, manufacturing, and select areas of the service sector. The goal is to draw foreign capital, technology, and expertise to improve the domestic industry's capabilities. As stated, all sectors that are not prohibited or do not fall under the "Permitted Sectors with FDI Limit" category are included in the Permitted Sector with 100% FDI.

- **Permitted Sectors with FDI Limit:** Foreign Direct Investment (FDI) is allowed in certain sectors, but only up to a particular percentage and often subject to specific conditions. These restrictions are intended to protect domestic industries, preserve competitive balance, or due to strategic reasons. For instance, in sectors such as broadcasting, banking, or defense, there may be limits on FDI (such as 49%, 74%, etc.) to ensure that control and decision-making largely remain in the hands of domestic entities or to protect national interests. These restrictions are frequently accompanied by additional regulatory mandates such as local partnerships, specific approval procedures, or operational guidelines.

Table No. 1: SECTOR-WISE FDI LIMIT IN INDIA

Sl. No.	SECTOR	FDI LIMIT	ENTRY ROUTE
1.	Banking- Public	20%	Government
2.	Banking- Private	74%	49%- Automatic. Above 49-74%- Government
3.	Insurance	74%	Automatic
4.	Asset Reconstruction Companies	100%	Automatic
5.	Credit Information Companies	100%	Automatic
6.	White Label ATMs	100%	Automatic
7.	Pension sector	49%	Automatic
8.	Agriculture & Animal Husbandry	100%	Automatic
9.	Plantation sector	100%	Automatic
10.	Mining	100%	Automatic
11.	Petroleum & Natural gas refining	100%	Automatic
12.	Defence manufacturing	100%	Automatic upto 49%. Above 49% under Government route.
13.	Broadcasting teleports	100%	Automatic
14.	Broadcasting content services	49%	Government
15.	Print media, dealing with news	26%	Government
16.	Publishing/printing of scientific and technical magazines/specialty journals	100%	Government
17.	Civil aviation- Airports	100%	Automatic
18.	Civil aviation- Air transport services	100%	Automatic up to 49% Above 49% under Government route.
19.	Telecom	100%	49%- Automatic. Above 49%- Government
20.	Railways	100%	Automatic
21.	Financial services' activities regulated by RBI, SEBI, IRDAI, other regulator	100%	Automatic
22.	Pharmaceuticals (Greenfield)	100%	Automatic
23.	Pharmaceuticals (Brownfield)	100%	Automatic upto 74%, above 74% under Government
24.	Power exchanges	49%	Automatic
25.	Construction development	100%	Automatic
26.	Industrial parks	100%	Automatic

27.	Satellites	100%	Government
28.	E-commerce activities	100%	Automatic
29.	Private security agencies	74%	Automatic up to 49%. Above 49%-74% under Government
30.	Single brand retail trading	100%	Automatic up to 49%. Above 49% under Government
31.	Multi-brand retail trading	51%	Government
32.	Duty-free shops	100%	Automatic
33.	Food products manufactured or produced in India	100%	Government
34.	Cash & carry wholesale trading	100%	Automatic
35.	Biotechnology	100%	Automatic
36.	Electricals machinery and system	100%	Automatic
37.	Food processing	100%	Automatic
38.	Ports and shipping	100%	Automatic
39.	Textiles and garments	100%	Automatic
40.	Tourism and hospitality	100%	Automatic

Source:*https://www.setindiabiz.com/sector-wise-fdi-limit-india*

As per Press Note 3 of 2020, foreign direct investment (FDI) from nations that share a land border with India, including China, Pakistan, Bangladesh, Afghanistan, etc. , is limited. This indicates that investment from these nations necessitates government consent, irrespective of the FDI limit in the relevant sector. The primary goal of this regulation is to avert opportunistic takeovers or acquisitions of Indian firms during periods of economic distress. Thus, it is vital for investors from these neighboring nations to comprehend the ramifications of Press Note 3 (PN-3) to successfully navigate the FDI procedures in India.

Technology Transfer and FDI

From the viewpoint of multinational corporations (MNCs), FDI is a tactical approach to leverage their technological capabilities by entering new markets. For host nations, it constitutes a chance to leapfrog technological levels and enhance competitive edge. The subsequent points explore the intricacies of these processes:

1. Establishment of Subsidiaries: MNCs frequently establish subsidiaries or joint ventures in host nations, bringing along proprietary technologies and methodologies.

2. Training and Skill development: An important element of technology transfer is the enhancement of human capital. MNCs often invest in training initiatives to improve the abilities of local employees, which may result in innovation spillovers.

3. Research and Development (R&D): FDI can encourage R&D endeavors within the host nation. Partnerships between foreign and local companies can lead to collaborative RandD projects, often backed by government incentives.

4. Supply Chain integration: By incorporating local businesses into their worldwide supply chains, MNCs convey process innovations and management practices.

5. Competition and Imitation: The entry of technologically advanced MNCs can heighten competition, motivating local firms to innovate and enhance their technologies. The presence of foreign banks in developing markets, for instance, has resulted in the uptake of advanced financial technologies by domestic banks.

6. Spillover Effects: Technology spillovers take place when local companies gain from the existence of MNCs without direct interaction. This can occur through observation, employee movement, or the demonstration effect. The pharmaceutical sector in India has experienced significant growth as a result of spillovers from the operations of foreign companies

7. Regulatory Frameworks and intellectual Property rights (IPR): The regulatory landscape of the host country is vital in facilitating technology transfer.

Market Size of The FDI In India

India's FDI inflows have surged nearly 20 times from 2000-01 to 2023-24, with cumulative inflows reaching approximately US$695.04 billion between April 2000 and June 2024, as reported by the Department for Promotion of Industry and Internal Trade (DPIIT). This remarkable growth can be attributed to government initiatives aimed at improving the ease of doing business and liberalizing FDI norms. In the most recent period from April 2023 to June 2024, India recorded FDI inflows of US$22.5 billion, with FDI equity inflows amounting to US$16.2 billion.

5. Data Discussion

- **FDI Inflow Over The Years**

Table No. 2: Year-wise FDI inflow data in India (From 2014-15 to 2023-24)(Amount in US $ Billions)

Sl. No.	**Year**	**Total FDI inflow**	**% growth over previous year (in USD terms)**
1	2014-15	45.15	(+)25%
2	2015-16	55.46	(+)23%
3	2016-17	60.22	(+)8%
4	2017-18	60.97	(+)1%
5	2018-19	62.00	(+)2%
6	2019-20	74.39	(+)20%
7	2020-21	81.97	(+)10%
8	2021-22	84.84	(+)3%
9	2022-23	71.36	(-)16%
10	2023-24	70.94	(-)1%

***Source**: Factsheet*

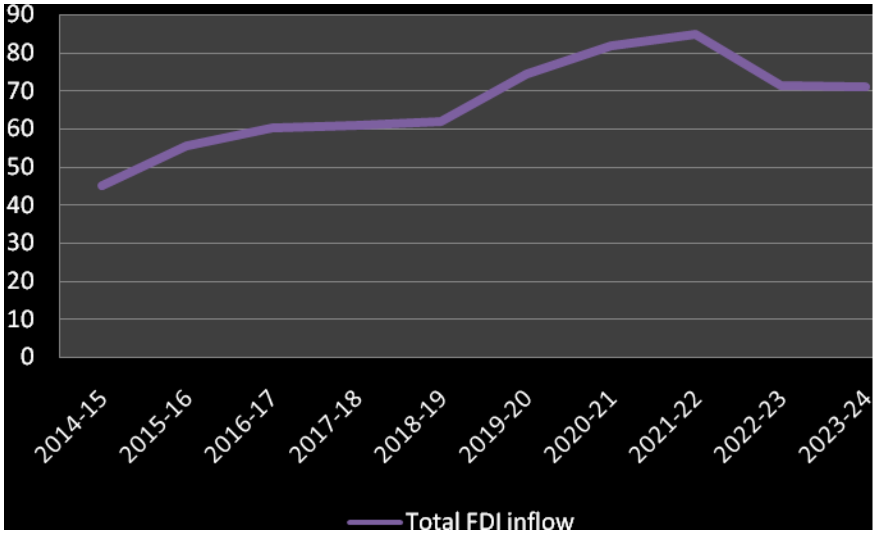

Figure 1: Year-wise FDI inflow data in India

Table No. 2 shows the year-wise FDI inflows in India from fiscal year 2014-15 to 2023-24. From 2014-15 to 2018-19, FDI inflows grew consistently, albeit at varying rate. The highest percentage increase was in 2014-15 at 25%. FDI inflow jumped to 20% in the year 2019-20, reaching $74.39 billion. There was continued growth in 2020-21 and 2021-22, but with smaller increases. FDI inflow increased in 2022-23 and 2023-24, with a 16% decline 2022-23, followed by a smaller 1% decrease in 2023-24.

- **Sector-Wise Inflow of FDI**

Table No. 3: Sector-wise equity inflow data in India (Amount in US *$Billions*).

Rank	Sector	FDI equity inflow	% of total FDI Equity inflow (in USD terms)
1	Services Sector	113.49	16%
2	Computer Software & Hardware	105.63	15%
3	Trading	43.86	6%
4	Telecommunications	39.78	6%
5	Automobile industry	36.66	5%
6	Construction (infrastructure) Activities	34.58	5%
7	Construction Development	26.64	4%
8	Drugs & Pharmaceuticals	22.76	3%
9	Chemicals (other than fertilizers)	22.71	3%
10	Non-conventional Energy	18.93	3%

***Source**: FDI Factsheet*

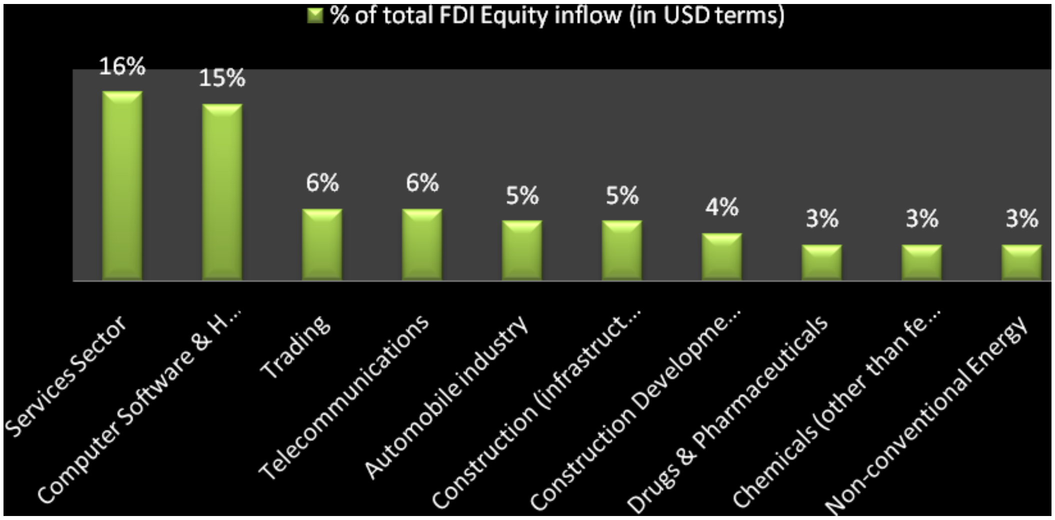

Figure 2: Sector-wise equity inflow data in India

Table No. 3 and figure 2 shows the Sector-wise equity inflow data in India. From April 2000 to June 2024, the Service sector attracted the highest FDI US$113.49 billion followed by computer software and hardware (US$105.63 billion), Trading (US$43.86 billion), Telecommunication (US$39.78 billion), Automobile industry (US$36.66 billion), Construction (infrastructure) Activities (US$34.58), Construction Development (US$26.64), Drugs & Pharmaceuticals (US$22.76), Chemicals (other than fertilizers)(US$22.71) and Non-conventional Energy (US$18.93)

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- **FDI EQUITY INFLOW OVER THE COUNTRIES**

Table No. 4: Country-wise FDI equity inflow *(Amount in US $Billions)*.

Rank	Country	Inflow	%of share
1	Mauritius	175.06	25%
2	Singapore	163.86	24%
3	USA	66.70	10%
4	Netherlands	51.13	7%
5	Japan	42.55	6%
6	United Kingdom	35.17	5%
7	UAE	19.06	3%
8	Cayman Islands	15.46	2%
9	Germany	14.74	2%
10	Cyprus	14.07	2%
Total		**695.04**	**-**

***Source**: FDI Factsheet*

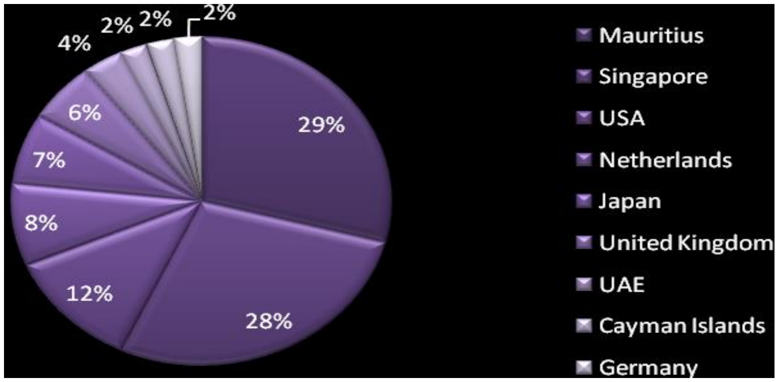

Figure 3: Country-wise FDI equity inflow

Table No. 4 and figure 3 represent the Country-wise FDI equity inflow of FDI from other countries. The highest FDI flow coming from Mauritius US$175.06 billion, followed by the Singapore (US$163.86 billion), USA (US$66.70), Netherland (US$51.13 billion), Japan (US$42.55 billion), United Kingdom (US$35.17), UAE(US$19.06), Cayman Islands (US$15.46), Germany (US$14.74) and Cyprus (US$14.07).

Table No. 5: State-wise FDI inflow *(Amount in US $Billions).*

Rank	Country	Inflow	%of share
1	Maharastra	77.57	31%
2	Karnataka	53.32	21%
3	Gujurath	40.22	16%
4	Delhi	33.01	13%
5	Tamil Nadu	11.94	5%
6	Haryana	10.43	4%
7	Telangana	8.86	3%
8	Jharkhand	2.67	1%
9	Rajastan	2.38	1%
10	Uttar Pradesh	1.68	1%

***Source**: Factsheet*

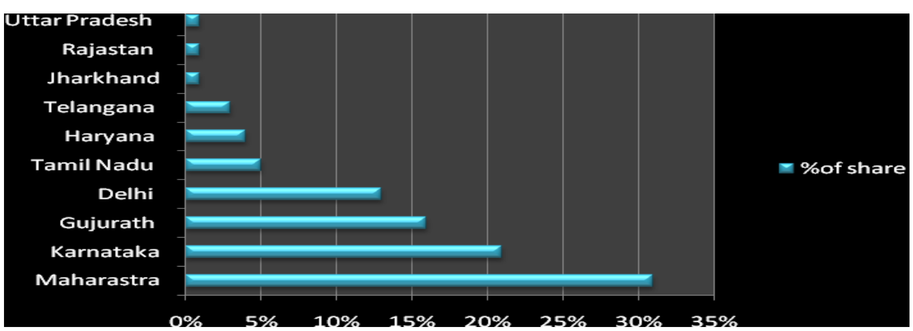

Figure 4: State-wise FDI inflows

Table No. 5 and figure 4 represent the state wise distribution of FDI in India. Regionally, Maharastra emerged as the top recipient of FDI equity inflows from October 2019 to June 2024, attracting US$77.57 billion. It was followed by Karnataka (US$53.31 billion), Gujurath (US$40.22), Delhi (US$40.22), Tamil Nadu (US$11.93 billion), Haryana (US$10.43 billion),Telangana (US$8.86), Jharkhand (US$2.67), Rajastan (US$2.38) and Uttar Pradesh (US$1.68). This distribution highlights the diverse regional appeal of India as a destination for foreign investment. India was the 3rd largest recipient of green field projects as per the World Investment Report 2023. The number of International project financial deals in India also increased by 64%, making it the second largest recipient of International project finance deals.

In 2022, India received 811 industrial investment proposals valued at approximately US$ 42.78 billion. Cumulatively, the total for the year reached around US$298 billion, a significant increase from 169.5 billion in 2021.

For Financial year 2023, India reported a foreign direct investment (FDI) inflow of US$ 71.35 billion while provisional figures for financial year 2024 indicate FDI worth US$70.95 billion. This reflects a strong interest in India's industrial sector and overall investment climate.

Government Measures to Increase FDI In India

India has successfully established itself as an appealing destination for FDI through a range of government initiatives. Here are some significant schemes and policies that have played a role in this trend.

- Make in India: Initiated in 2014, this program aims to motivate companies to produce goods within India. It fosters investment across various sectors such as manufacturing, defense, and aerospace
- Startup India: This program assists startups by offering easier access to funding, tax exemptions, and a streamlined regulatory environment, drawing in both domestic and foreign investor
- FDI Policy Reforms: The government has progressively relaxed FDI regulations in numerous sectors, including defense, retail, and aviation, permitting greater foreign ownership and facilitating the approval process
- Digital India: This program aims to convert India into a digitally empowered society and knowledge economy, enticing tech-related investment
- National Infrastructure Pipeline (NIP): Launched in 2019, NIP is designed to enhance infrastructure and draw investments in sectors such as transportation, energy, and key sectors, encouraging investments from both domestic and foreign entitie
- Sector-Specific Initiatives: The government has introduced targeted programs for areas such as renewable energy, healthcare, and tourism to lure FDI by providing incentives and fostering a supportive environment

- Atmanirbhar Bharat (Self-Reliant India): This initiative intends to enhance local manufacturing and decrease reliance on imports, attracting FDI in critical sectors like defense, agriculture, and pharmaceutical
- Foreign Investment Promotion Board (FIPB): Although the FIPB has been dissolved, the government has simplified the FDI approval process, making it more transparent and accessible for foreign investor
- Production-Linked Incentive (PLI) Scheme: This scheme provides incentives to manufacturers in essential sectors to boost domestic production and attract foreign investment.

6. Conclusion

FDI is becoming a significant global hub for FDIs. FDI plays a vital role in India's economic development, propelling growth, job creation,and imparting technological. The Government's major initiatives such as, "Make in India," "Startup India," and various sector-focused reforms have fostered a more favorable investment landscape, attracting global investors.As India continues to liberalize its FDI regulations and improve infrastructure, it is ready to emerge as a key player in the international market. By nurturing a stable and transparent business environment, India can further leverage FDI to accelerate its economic transformation and achieve sustainable development.

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