

A Study of Relationship between FDI Inflow and Economic Growth in India

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Abstract

Foreign Direct Investment (FDI) is a financial capital instrument which is the idlest way of capital inflow in any economy. FDI play an important role in economic growth of the country by filling the gap between domestic investments and savings. Many world economies including India have obtained financial benefit from FDI inflows for their economic growth. This study shows the trends of foreign direct investment (FDI) and Economic growth of the country. An attempt has also been made to find out the relationship between them during the study period from 2000-2001 to 2017-2018.

Keywords: Foreign Investment, Economic Growth.

INTRODUCTION

Foreign investment is an important element of economic growth for economy. But in the context of developing and under developed countries it becomes more important. The attractive features of these developing countries are that these have not proper amount of capital which must be required to support the growth of the economy. In such situations foreign investment is required for filling the gap between the available resources and the required resources. It provides a better opportunity to the country in long term development not providing as a resources of capital but for encouraging competition in economy through the exchange of technology, boosting output and also creating new employment opportunity. In India foreign investment is assumed as a development technique. That will aid different sectors and overall growth of the country.

Foreign investment considers as a form of capital budgeting. Through the foreign investment a country receives the capital for development purpose. While domestic investment brings addition in capital stock of an economy, foreign direct investment represents a corresponding role in filling the gap between domestic saving and investment. At the macro level foreign investment is considered as a non-debt creating sources of additional or surplus external finance. At the micro level foreign investment is considered to raise output or production, innovative technology, skills, employment and linkages or we can say relationships with other sectors of the domestic country.

Foreign investment affect the economic growth of host country through the transfer of technology, human resources formation, integrating the global markets, encouraging the competition and firm development and restructuring. Empirically different studies consider that foreign investment encourage the economic growth in the host country.

Review of Literature

Anitha R. (2012) have presented the article on FDI and economic growth in India and suggested that FDI has a great importance in the long term development of a country. Alfaro L. (2003) in his study concluded that FDI has the negative effect on service sector and put the positive effect on manufacturing sector. Khaliq A. (2007) concluded that FDI inflow have positive impact on the economic growth of the country. Waser, C. (2012) have analysed the impact of foreign investment on economic growth and suggested with the help of regression analysis that there is a positive relationship between the foreign investment and economic growth. Solomon, E.M (2011) in his study analysed the impact of foreign investment and other economic factor by using econometric technique and suggested that foreign investment and other economic factor positively affect the economic growth of the country. Kapoor S. (2015) had studied the impact of FDI and FII on the Indian stock market by using correlation and regression analysis. He found that the flow of FDI has no significant impact on stock market but FII in India determine the trend of Indian stock market. Simionescu M. (2016) in his study analysed the relationship of economic growth and foreign direct investment during the economic crisis in European Union. For this purpose he used the panel data approach and Bayesian technique from the period of 2008 to 2014 data. He found that in the European Union, economic growth and FDI shared the reciprocal relationship since the beginning of the crisis with a tendency to reduce disparities between countries in attracting FDI. Carp L. (2012) made a literature review study on the analysis of relationship between FDI and Economic Growth and highlight the significance of the FDI inflows on the host country's economic growth through the theoretical and empirical research for the approached field. He found that the FDI flow impact on economic growth is significant. Kumar R. (2014) in his study suggested models to analyse the contribution of FDI on economic growth of the country. The study found that FDI inflow is the most important variable which influence the level of economic growth. Karnika & Garg (2015) examined the time lag required for FDI to make its utmost impact on economic growth in India. For the purpose of the study, data on FDI and GDP for the period 2000-01 to 2012-2013 are analysed by using by using lag regression model. The study confirms that FDI requires atleast three years to make its contribution to the economic growth in a significant and utmost favourable manner. They concluded that there is a need for the regular rise in FDI to bring continuous in economic growth.

Objectives of the Study

Following are the objectives-

- To study the trend of GDP and Net FDI in India for the last eighteen year.
- To examine the relationship between FDI inflow and GDP in India.

Research Methodology

This study is exploratory cum descriptive in nature. The secondary data has been collected by various authenticated sources i.e. Reserve Bank of India bulletin, publications from Ministry of Commerce and industry etc. It is a time series data that has been collected for the period from 2000-01 to 2017-18. With the aim of analysing the data, statistical tools and graphs has been used.

Foreign Direct Investment Inflow during the period of 2000-01 to 2017-18 in India

The first objective of this study is to see how the foreign investment affects the economic growth and for this purpose we analyse the magnitude of FDI inflow from 2000-01 to 2017-18.

Table 1

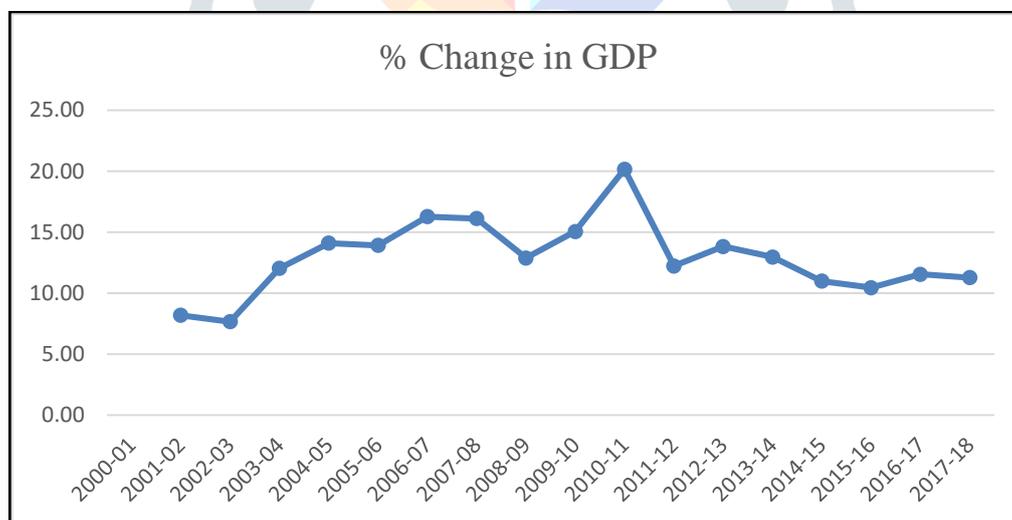
Trends of FDI And GDP in India During 2000-01 to 2017-18

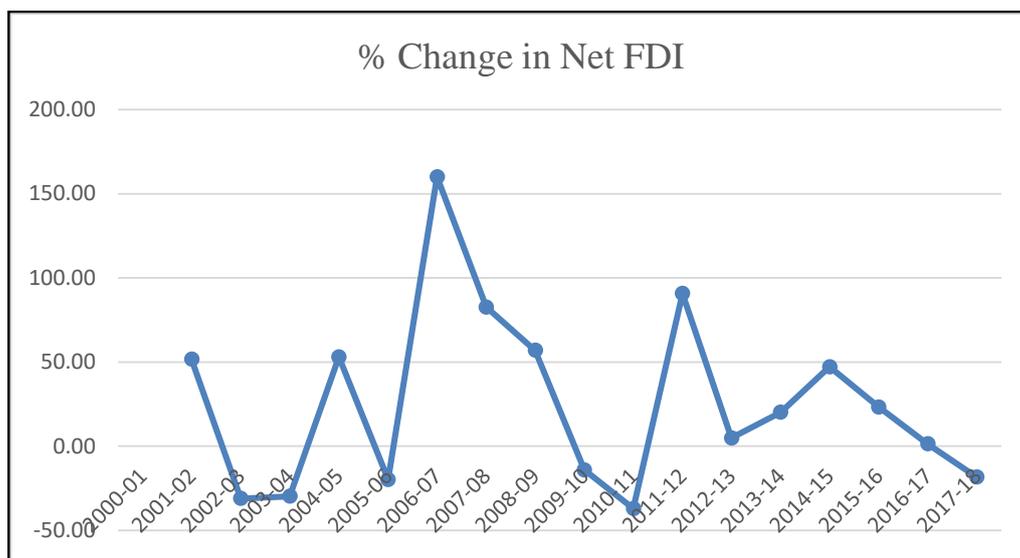
Years	GDP		Net FDI	
	in Rupees Billions	% Change	in Rupees Billions	% Change
2000-01	21774.13	-	149.24	-
2001-02	23558.45	8.19	226.30	51.63
2002-03	25363.27	7.66	155.94	-31.09
2003-04	28415.03	12.03	109.44	-29.82
2004-05	32422.09	14.10	167.45	53.01
2005-06	36933.69	13.92	134.25	-19.83
2006-07	42947.06	16.28	349.10	160.04
2007-08	49870.90	16.12	637.76	82.69
2008-09	56300.63	12.89	1001.06	56.96
2009-10	64778.27	15.06	859.83	-14.11
2010-11	77841.15	20.17	541.01	-37.08
2011-12	87363.29	12.23	1031.67	90.69
2012-13	99440.13	13.82	1081.86	4.86
2013-14	112335.21	12.97	1299.69	20.14
2014-15	124679.59	10.99	1912.19	47.13
2015-16	137718.74	10.46	2357.82	23.30
2016-17	153623.86	11.55	2389.13	1.33
2017-18	170950.05	11.28	1950.52	-18.36

Source: Handbook of Statistics on Indian Economy (2017-18) and Researchers Calculations

After analysed the table 1 we find out that the FDI inflow in India during the period of 2000-01 to 2016-17 mostly in favour in Indian economy. Although in some years the trends of foreign investment inflow in India was negative but the growth rate in other years has compensated it. Table 1 also revealed that, GDP has continuously increasing over the years: however the rate of increase varies across the years. On the other hand FDI inflow shows the tendency of ups and down during the study period. In 2001-02 the flow of FDI rose speedily (51.63%), but after that it started falling for the coming two years. The spectacular rise in FDI has been shown in the year 2006-07 which was greater than two and half times as compared to previous year. In 2006-07 there was also an increase in GDP (16.28%) than the previous year. It may be due to the rise in FDI inflow. In 2007-08 and 2008-09 FDI inflow is again increasing but after that it declined till 2010-11 i.e. 37.08%. After that, it has shown a considerable increment in 2011-12 .Meanwhile, the increment in GDP remained continue. It is probably due to the influence of FDI inflow of current and past years. In 2012-13 the FDI inflow is again showing negative growth as compared to the previous year. But after 2010-11 the total inflow of FDI again started increasing till 2015-16. This increase in FDI inflow is may be due to introduction of various policies like Make in India, and other policies which results in increasing the FDI shares in different sectors by the ongoing government. However , As compared to the year 2016-17 GDP has shown an increment by 11.28% in 2017-18 and on the other hand, Net FDI has been decreased by -18.36% as compared to 2016-17 which is clearly shown in the following figures.

Figure 1: Movement in GDP and FDI inflow during 2000-01 to 2017-18





Source: Prepared from data given in table 1

Figure 1 shows the percentage change in Net FDI inflow and GDP growth rate from the period 2000-01 to 2017-18. It is seen from the above figure that there is an increasing trend of GDP and fluctuating trend of Net FDI inflows. It become clear from the above figure that GDP has higher growth rate in 2010-11 while FDI has highest percentage growth in 2006-07, but expansion path of GDP is looking smooth as compared to FDI. In spite of getting considerable increase in FDI inflow, it has faced diminishing trends for years and continued till 2017-18. FDI has shown a major rise and fall in the years 2006-07 and 2010-11 respectively. Despite of decrease in FDI in the year 2010-11, there was a significant rise in GDP

Table-2:

Correlation Matrix

	GDP	Net FDI
GDP	1	0.949196
Net FDI	0.949196	1

Source: Calculation based on data available.

Table. 2 shows that Net FDI inflow is positively related to economic growth of the country and there is high degree of linear relationship between them which means that with increase in FDI, GDP also increases. The results indicate that in India’s economic growth FDI has great contribution.

Conclusion

After analysed the study material and review of literature we concludes that foreign investment inflow and economic growth is connected to each other and was favourable to Indian economy. Although in few years the foreign investment inflow was negative in India but the great increase in other years

compensates it and provides various benefits to Indian economy. The results of correlation shows that there is a high degree of linear relationship between GDP and FDI inflow. The present study also reveals that there is a need to encourage the foreign direct investment every year to enhance economic growth in Indian economy. For that government of India should improve the investment climate for foreign capital through the maintenance of political as well as economic stability along with curbing corruption. Moreover, by providing adequate market size, easy accessibility to export market, developed infrastructure, cost-effectiveness and by other means more FDI can be attracted. Along with this, there is a rationale for the adoption of innovative as well as advanced policies and good governance practices on par with international standards to make India as a most preferred destination for foreign capital.

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