

# Role of Foreign Direct Investment in Service Sector

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**Abstract :** The concept of Foreign Direct Investment is now a part of India's economic future but the term remains vague to many, despite the profound effects on the economy. Despite the extensive studies on FDI, there has been little illumination forthcoming and it remains a contentious topic. FDI is an integral part of an open and effective international investment architecture matter for attracting FDI to a large number of developing countries and for reaping the full benefits of FDI for development. Many policy makers and academics contend that FDI can have important positive effects on a host country's development efforts. In addition to the direct capital financing it supplies, FDI can be a source of valuable technology and know-how while fostering linkages with local firms, which can help jumpstart an economy. FDI eludes definition owing to the presence of many authorities; Organization for Economic Co-operation and Development (OCED), International Bank For Reconstruction And Development (IBRD), International Monetary Fund (IMF), and United Nation Conference on Trade and Development (UNCTAD). All these bodies attempt to illustrate the nature of FDI with certain measuring methodologies. Generally speaking FDI refers to capital inflow from abroad that investment in the production capacity of the economy and are "usually preferred over other forms of external finance between because they are non-volatile and their returns depend on the performance of the projects financed by the investors. FDI also facilitates international trade and transfer of knowledge, skills and technology." This paper shows that the benefits of FDI vary greatly across sectors by examining the effect of FDI on growth in the service sectors.

**IndexTerms - FDI, Positive effects, Development efforts, Valuable technology, Performance.**

## I. INTRODUCTION

The concept of Foreign Direct Investment is now a part of India's economic future but the term remains vague to many, despite the profound effects on the economy. Despite the extensive studies on FDI, there has been little illumination forthcoming and it remains a contentious topic. FDI is an integral part of an economic and effective international economic system and a major catalyst to development. FDI to developing countries in the 1990 was the leading source of external financing and has become a key a key component of national development strategies for almost all the countries in the world as a vehicle for technology flows for attaining competitive efficiency by creating a meaningful network of global interconnections. FDI provides opportunities to host countries to enhance their economic development and opens new opportunities to home countries to optimize their earning by employing their ideal resources. India's rank fifteenth in the service output and its provides employment to around 23 percent of the total work force in the country. The contribution of the service sector to the Indian economy has been modified; a 55.2 percent share in FDI interflows and occur one third of total export growth through the first half of 2010-11. The various sectors under the service sector in India are construction, trade hotels, transport, restaurant, communication and storage, social and personal service, community, insurance, financing, business and real estate.

## II. OBJECTIVE

1. To study the FDI inflows in Indian service sector from 2000-2010.
2. To study the relationship between service sector growth and Indian economy.

## III. METHODOLOGIES OF THE STUDY

The study is based on secondary sources of data. The main sources of data are various Economic surveys of India. RBI bulletins, journals, articles, newspaper etc.

#### IV. IMPORTANT SERVICES FOR INDIA

Some services have been particularly important for this improving performance in India. Software is one sector in which India has achieved a remarkable global brand identity. Tourism and travel related services are also major items in India's services include many professional services, infrastructure-related services and financial services.

**TABLE-1**

Share of different categories in GDP at factor cost (constant price) in percentage

Sectors	2005-06	2006-07	2007-08	2008-09	2009-10
<b>Trade, Hotels &amp; Restaurants</b>	<b>16.7</b>	<b>17.1</b>	<b>17.1</b>	<b>16.9</b>	<b>16.3</b>
Trade	15.1	15.4	15.4	15.4	14.3
Hotel & Restaurants	1.6	1.7	1.7	1.5	2.0
<b>Transport, storage &amp; Communication</b>	<b>8.3</b>	<b>8.2</b>	<b>8.0</b>	<b>7.9</b>	<b>8.8</b>
Railways	0.9	0.9	1.0	0.9	1.0
Transport by other Means	5.7	5.7	5.5	5.5	5.2
Storage	0.1	0.1	0.1	0.1	0.1
Communication	1.6	1.5	1.4	1.4	1.4
<b>Financing, Insurance Real estate &amp; business services</b>	<b>14.5</b>	<b>14.8</b>	<b>15.1</b>	<b>16.1</b>	<b>16.1</b>
Banking, Insurance	5.4	5.5	5.5	5.7	5.4
Real estate, ownership Of dwelling & business services	9.1	9.3	9.6	10.4	11.4
<b>Community, social &amp; Personal services</b>	<b>13.54</b>	<b>12.8</b>	<b>12.5</b>	<b>13.3</b>	<b>14.4</b>
Public administration & defense	5.6	5.2	5.1	5.8	6.3
Other services	7.9	7.6	7.4	7.5	8.1
<b>Construction</b>	<b>7.9</b>	<b>8.2</b>	<b>8.5</b>	<b>8.5</b>	<b>8.2</b>
<b>Total services (excluding construction)</b>	<b>52.9</b>	<b>52.9</b>	<b>52.7</b>	<b>54.1</b>	<b>55.2</b>
<b>Total services (including construction)</b>	<b>60.8</b>	<b>61.1</b>	<b>61.2</b>	<b>62.6</b>	<b>63.4</b>
<b>Total GDP</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>

SOURCE:-eso

**TABLE-2**

*Number of Greenfield FDI projects in service industries 2007-2009*

SECTOR	2007	2008	2009
Hotel & Tourism	297	553	370
Transport, Storage and Communications	1024	1269	1133
Communications	448	594	544
Financial Services	1161	1616	1267
Business services	2922	3647	2927

Source:- UNCTAD, WIR, 2010,

#### V. FOREIGN DIRECT INVESTMENT AND ECONOMIC GROWTH

The IMF definition of FDI includes many as twelve different elements-equity capital, reinvestment earning of foreign companies, intercompany debt transactions short terms and long term loans, financial leasing, trade credits, grants, bonds non-cash acquisition of equity, investment made by foreign venture capital investors, earning data of indirectly held FDI enterprises, control premium and non-competition fee. India, however, does not adopt any other element other than equity capital reported on the basis of issue of transfer of equity of preference shares to foreign

direct investors. So far Indian economy has been heavily geared towards the service sector that contributes 56% of our GDP. The services contribution to the increase in GDP over the last 5 years has been 63.9% having a contribution from services is an attribute that is characteristic of developed economics.

### Service sector contribution to the Indian economy

The service sector contributes the most of the Indian GDP. The sector of services in India has the biggest share in the country's GDP for it accounts for around 53.8% in 2005. The contribution of the services sector in India GDP has increased a lot in the last few years. The services sector contribution 15% to the Indian GDP in 1950s. Further the Indian services sectors share in the country's GDP. The contribution of the services sector has increase very rapidly in the Indian GDP for many foreign consumers have shown interest in the country's service exports. This is due to the fact that India has a large pool of highly skilled, low cost and educated workers in the country. The foreign companies seeing this have started outsourcing their work to India especially in the area of business services which includes business process outsourcing and information technology services. This has given a major boost to the services sector in India, which in its turn has made the sector contribute more to the India GDP.

### Trends and patterns of FDI inflows in Indian service sector

Table-3 present year wise FDI inflows in service sectors form 2000-2005. In flows of FDI in India has been uniform across all services sector. Growth in FDI flows are found to be the heaviest in consultancy services, financial and non financial services, Hotel and Tourism and Telecommunications and Trading, consultancy services records a highest growth of 119.0% per annum during study period. FDI in financial and non financial services, hotel and tourism and telecommunication and trade record a growth trade record a growth rate of 60.5, 46.8, 43.9, 32.0 percent per annum respectively.

**Table-3**

SECTOR	2000	2001	2002	2003	2004	2005
Telecommunication	6855.4	4267.1	9090.7	7272.6	6087.84	9639.13
Consultancy Services	209.0	2922.9	1003	2480.3	11843.5	1627.16
Financial	1861.5	5202.2	15431.4	13904.0	11455.83	31445.14
Non-financial	524.0	471.5	2237.9	2594.2	1527.23	2799.59
Hotel & Tourism						
Trading	1239.8	2204.4	1824.2	831.5	682.16	1257.67
Total Service	10689.7	56472.1	29587.2	27082.6	31596.56	46768.69
Total FDI Inflow	193417.0	192652	212860	143011	172657.5	192990.9

Many policy makers and academics contend that FDI can have important positive effects on a host Country's development effort. In addition to the direct capital financing it supplies, FDI can be a Source of valuable technology and Know-how while fostering linkages with local firms, which can help jumstart on economy. Based on these arguments, industrialized and developing countries have offered incentives to encourage foreign Direct Investment in their economics.

## **V. FOREIGN DIRECT INVESTMENT CULTURE**

Many economists in the country have now realized the advantages of FDI to India. While the achievements of the Indian government are to be lauded, a willingness to attract FDI has resulted in what could be termed an "FDI Industry". While researching the economic reforms on FDI, it was discovered that there exists a plethora of boards committees, and agencies that have been constituted to case the flow of FDI. Reports from FICCI and the planning commission place investor confidence and satisfaction at an all time high, citizens too deserve to be clued in on the government bodies are doing. All proposals for foreign Investment Promotion Board. The FIPB also grants composite approvals involving foreign investment/foreign technical collaboration.

## VI. FINDINGS AND CONCLUSION

1. Foreign Direct Investment is an important stimulus for the economic growth of India.
2. Foreign Direct Investment a tremendous growth in second decade (2000-2010) that is three times then the first decade of FDI in service sectors.
3. Banking and Insurance is first and Telecommunication is second segment of service sector which pick the growth in second decade of reforms.
4. Foreign Direct Investment creates high perks jobs for skilled employee in Indian Service Sector.

As evidence by analysis and data the concept of FDI has evolved from the shadow of shallow understanding to proud show of force. The Government while serious in its efforts to include growth in the economy and country started with foreign investment in a haaphazaed manner. Liberalization of services involves potential advantages for Indian economy. Benefits can arise from increase competition, lower prices and better quality of services. FDI in services provide key inputs to other productive activities that lead to further investment and competitiveness of an economy. Indian service sector is generating the proper employment options for skilled workers with high perks. The decisions governing FDI have been spread over many areas and agencies that have to be streamlined or overreaching regulatory body and practical policy has to be developed. This paper finds that FDI flow into the different sectors of an economy exert different effects on economic growth. Foreign Investment in the service sector has an ambiguous effect. The economic nature of the host country is also an important determinant.

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