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Overseas Direct Investment and its Economic Impact in India

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Abstract: Indian economy is a developing economy that is ranked as the sixth-largest economy of the world, as per nominal Gross Domestic Product (GDP) and the third-largest by purchasing power parity (PPP). India achieved a 6-7% average GDP growth annually. Foreign direct investment in India is a major monetary source for economic development in India. This paper includes the research involving Indian FDI outflow and its economic impact. The tools used for the study includes the time series analysis and trend analysis for analyzing the FDI outflows for a time span of 13 years from 2005 to 2016. The Karl Pearson's Co-efficient of Correlation and the Coefficient of determination are the tools used for analyzing the correlation that exists between FDI outflows and three major economic factors, namely exports, imports and GDP. The average FDI inflows during the last decade were observed to be US$ 31.58 billion, whereas the outflows averaged to US$ 11.02 billion. The research has proved that ODI does not have direct relationships between any of the economic factors, i.e. exports, imports and GDP. It is one of the avenues that the country's MNCs can peruse as an expansion tool for capturing the overseas market.

Keywords: Economic Impact, Exports, GDP, Imports, OFDI, Overseas Direct Investment

I. INTRODUCTION

In the era where changes seems to be occurring at a very high rate, whether it is the economic reforms in the country, or the way business is run by the companies, or it is the way the rules and regulations are revolutionized for a better tomorrow, development is naturally inevitable. There are innumerable factors, economic as well as non-economic, that lead to the development seen in India over the recent past. Some of the economic factors that contribute a larger share to the country's development include the Natural Resources, Capital Markets, Exports and Imports, Capital Formation and the Economic system as a whole.

Indian economy is a developing economy that is ranked as the sixth-largest economy of the world, as per nominal Gross Domestic Product (GDP) and the third-largest by purchasing power parity (PPP). According to the International Monetary Fund (IMF), as one of the world's fastest-growing economies, accounting for about 15 percent of global growth, India's economy has helped to lift millions out of poverty. India achieved a 6-7% average GDP growth annually. In Financial Year 2015 and 2017 India's economy became the world's fastest growing major economy overtaking China. It is estimated that the country is expected to be a USD 6 trillion economy -- the third largest in the world by 2027, majorly because of digitization. It is also prominent to observe that almost two-thirds of the total population in India is of working age (between 15 and 64) and thus it is time to reap the demographic dividend for further growth.

Among all the economic factors leading to the smooth running of the economy, Foreign Direct Investment (FDI) is a major contributor for the development in India. Foreign direct investment in India is a major monetary source for economic development in India. Foreign companies invest directly in fast growing private Indian businesses to take benefits of cheaper wages and changing business environment of India.

The OECD Benchmark Definition of Foreign Direct Investment (Fourth Edition, 2008) states that, "FDI provides a means for creating direct, stable and long-lasting links between economies. Under the right policy environment, it can serve as an important vehicle for local enterprise development, and it may also help improve the competitive position of both the recipient ("host") and the investing ("home") economy. In particular, FDI encourages the transfer of technology and know-how between economies. It also provides an opportunity for the host economy to promote its products more widely in international markets. FDI, in addition to its positive effect on the development of international trade, is an important source of capital for a range of host and home economies".

Foreign Direct Investment is seen to be promoted by the Government of India for the enhancement of domestic capital, securing latest technology and skills and for increasing economic growth. According to the BCG Globalisation Readiness Survey, (BCG Analysis)

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Multinational companies consider the BRIC Nations and Southeast Asia Markets important for their strategy formulation. India stands second in the preferences among the nations along with Brazil preceded by China taking the first priority. Indian companies for promoting global business are undertaking many overseas investments in the form of Joint Ventures (JV) and Wholly Owned Subsidiaries (WOS). Whether it is a JV or a WOS (or even financial commitments) it is considered as a means of economic and business cooperation between the host and the home country since it lead to a lot of benefits that include R&D, technology transfer, employment generation, skill sharing, and may more.

There are two aspects of FDI policy framework that are generally adopted by the countries. One is the Inflow of FDI in the country and the other is Outflow of FDI by the country. This paper tries to study the FDI outflow that is undertaken by India and also try to comprehend the significance of this concept at a macro level. The tools used for the study includes the time series analysis and trend analysis for analyzing the FDI outflows for a time span of 13 years from 2005 to 2016. The Karl Pearson's Co-efficient of Correlation and the coefficient of determination is another statistical tool used for analyzing any correlation that exists between FDI outflows and three major economic factors, namely exports, imports and GDP.

According to the data provided by Reserve Bank of India (RBI), India's outward Foreign Direct Investment (OFDI) in equity, loan and guaranteed issue stood at US$ 784.28 million in the month of February 2018 as against US$ 866 million in January 2018 and US$ 1.35 billion in February 2017. Indian overseas investment policies has been progressively liberalized and simplified to meet the changing needs of a growing economy. The policy, which was evolved as one of the strategies for export promotion and for strengthening economic linkages with other countries, has expanded significantly. Outflows from India, the main source of FDI in South Asia, more than doubled to $11 billion. India's State-owned oil and gas company ONGC has been actively investing in foreign assets in recent years.

II. RESEARCH METHODOLOGY

This study has focused on the trend of OFDI by India and also focused on the economic factors that may or may not be related to each other. For analyzing the data of FDI outflows, fitting of a straight line trend, using the method of least squares, was adopted and applied to the statistics collected for the 13 years FDI outflows in India. The equation used for fitting the straight line trend is $Y = a + bX$. Where X is the time period (Year), Y is the value of ODI over the years, 'a' and 'b' are coefficients used to form the slope of the curve (trend line). The equation to fit the trend line: $Y = a + bX$ [$Y = 11.02 - 0.50 X$]

This section undertakes an analysis to measure and conclude the impact and relation that other macro economic factors have on Overseas Direct Investment in India. The research aims to study the economic factors which include Exports, Imports and GDP. The current analysis uses the Karl Pearson's Coefficient of Correlation model. The model intends to study the correlation between ODI and exports, ODI and imports and lastly ODI and GDP. The results are put forth accordingly. Table 1 lists the figures relating to the FDI outflows and the economic factors used for the analysis. After applying the correlation model, the coefficient of determination was also used for analyzing the generated value of 'r' (correlation coefficient).

III. OVERSEAS DIRECT INVESTMENT FROM INDIA (LITERATURE REVIEW)

The development and evolution of Overseas Direct Investment in India has been consistent right from the pre-liberalization period. The evolution of the overseas investment policies in our country can be classified into two distinct phases, the pre 2003 and the post 2003 phase. The pre 2003 phase being export oriented with cash flow restrictions and the post 2003 phase where the automatic route was liberalized that allowed Indian firms to invest abroad up to 200% of their net worth in a year. (Keynote address by Mrs. Shyamala Gopinath, Deputy Governor of the Reserve Bank of India, at the International Conference on Indian cross-border presence/acquisitions, Mumbai, 19 January 2007). The development can not only be seen by the policy changes but also the geographical spread and sectorial composition of the overseas direct investments taking place by Indian Multinationals in various markets abroad.

Dr. O.S. Doel (2017) has pointed out the pattern and composition of global outward foreign direct investment that has changed during last two decades. And it was observed that Indian companies prefer making outward foreign direct investments in the economies where chances of economic growth are better and government is effective in controlling corruption and malpractices.

Dilip Saikia (2012) has explained that the large scale of outward FDI from India has both the positive and negative impacts at both the micro level of firms and macro level for the country. Positive impacts include market access for exports, opportunities for integration, upgrading and developing technology, acquiring international brand names, etc. and negative impacts include increased costs, lower profits higher debts and overstretched finances, etc.

Supriya Chopra and Satvinder Kaur Sachdeva (2014) concluded that outward FDI relates to multilayered structures. The motivations range from genuine business/commercial considerations to taxation benefits which are available to any global investors.

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Ravi Subramanian, Charu Sachdeva & Sebastian (2010) FDI outflows from India have accelerated only in the last decade post liberalization. It has been found that firms, in the early part of their "invest abroad" cycle with little experience tend to form alliances or joint ventures while venturing into a foreign market but gradually move towards Greenfield acquisitions after gaining experience into markets abroad.

The changing scenario in the overseas investment destinations in the past few years is also worth noting. India Brand Equity Foundation in their article 'Indian Investment Abroad - Overseas Direct Investment By Indian Companies' (2018) have rightly pointed out that earlier the focus of the overseas investment was towards nations with good resources such as Australia, UAE, and Sudan. But in the recent past the change is visible from the pattern of countries where Indian MNCs (Multi National Corporations) are investing in countries with good tax benefits such as Mauritius, Singapore, and the Netherlands.

The growth of the Overseas Direct Investment can be attributed to the opportunities that the MNCs seek for growth, liberalized guidelines, technology transfers, enhanced funding sources, access to new markets and for global reach. Ronny Thomas and K. Narayanan, 2013 proved OFDI firms on an average produces more output, labour and capital intensive compared to exporting firms. Exports are significant and positive determinant of OFDI of firms in the Indian manufacturing industry.

The RBI has also liberalized guidelines for foreign investments abroad by Indian companies by raising the annual overseas investment ceiling to US$ 125,000 from US$ 75,000 to establish JV (Joint Venture) and WOS (Wholly Owned Subsidiaries). The government's supportive policy regime complemented by Indian firms' experimental outlook could lead to an upward trend in OFDI (Outflow of Foreign Direct Investment) in future.

IV. RESEARCH ANALYSIS

The study undertook a detailed analysis for studying the foreign direct investment outflows and the economic factors, exports, imports and GDP. Table1 puts forth the values of all the data collected for the analysis.

Table 1: Statistics for FDI, Exports, Imports and GDP in India

Year	Fdi Outflows*	Exports*	Imports*	GDP (%)
2005	2.64	100.35	140.86	9.28
2006	14.04	121.20	178.21	9.26
2007	17.03	145.90	218.65	9.80
2008	19.26	181.86	315.71	3.89
2009	16.10	176.77	266.40	8.48
2010	15.97	220.41	350.03	10.26
2011	12.61	301.48	462.40	6.64
2012	8.55	289.56	488.98	5.46
2013	1.77	336.61	466.05	6.39
2014	11.69	317.54	459.37	7.51
2015	7.52	264.38	390.74	8.01
2016	5.05	260.33	356.70	7.11
2017	11.09	298.38	447.24	6.20

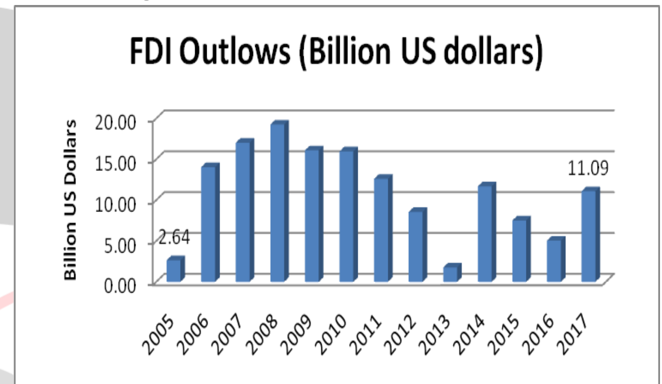
**Figures expressed in Billion US dollars;*

Source: Data compiled from UNCTAD, OECD and RBI Statistics

Application of Trend Analysis:

Figure 1 reveals the picture of the Overseas Direct Investments (in billion US$) for a span of 13 years. There is seen a very uneven flow of OFDI spread over the years under study. The trend analysis for this data illustrates that the ODI over the time span considered depicts a declining trend.

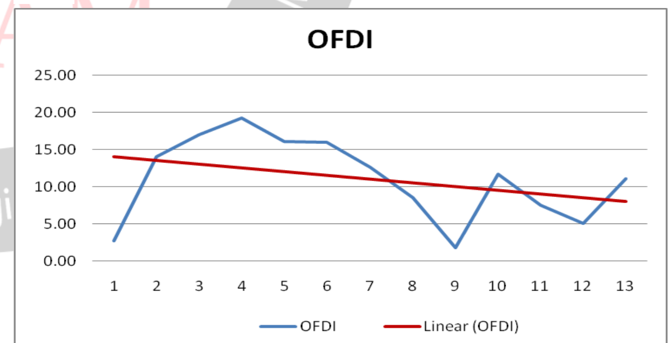
Figure 1: Overseas Direct Investment



Source: Data compiled from OECD, UNCTAD and RBI

As shown in Figure 2. Unless favorable measures are taken and there is shift in the scenario for ODI encouragements, it is assumed that the pattern of overseas investments undertaken by India, which show a negative growth trend, may continue even further.

Figure 2: Straight Line Trend for the values of ODI in India



Source: Statistics compiled from UNCTAD, OECD and RBI Statistics

Application of the Correlation and Coefficient of Determination

For the study, the FDI outflows were considered as variable X and Exports, Imports and GDP were considered as variable Y (using three different models/cases), for conducting the analysis. For the first case: correlation between ODI and exports; second case: correlation between ODI and imports and third case: correlation between ODI and GDP was analyzed.

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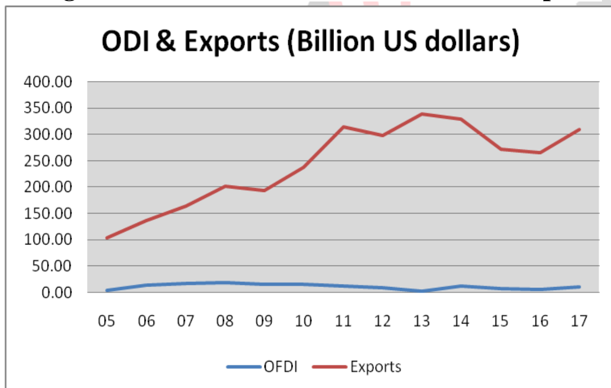
CASE 1: Correlation between ODI and Exports:

In the first part of the analysis, the correlation between ODI and exports was analysed. Here, the overseas direct investments were considered as X and exports were considered as Y. Thus the values obtained for the coefficient calculation were: The correlation coefficient (r) for the data set was -0.323, and the coefficient of determination (r^2) was 10.43%. The value of r shows that the correlation between the two variables considered is almost equal to zero. It is termed as zero correlation. As the figure 3 clearly portrays, it can be concluded that the two variables, ODI and exports are not correlated to each other. Whatever change happens in ODI, it has no impact on the exports in the country. Both the variables share a random, non-linear relationship. The coefficient of determination also shows that 10.43% total variation in exports can be attributed to the relationship with the overseas direct investment, which is a very small amount that does not imply any major change factor. Thus there is no correlation between ODI and exports. It can be concluded that firms undertaking OFDI are not directly related to the exporting firms. Productive firms undertake Outward Foreign Direct Investment (OFDI) compared to firms which chose exports as mode of internationalization (Ronny Thomas and K. Narayanan, 2013).

Figure 3: Overseas Direct Investments & Exports

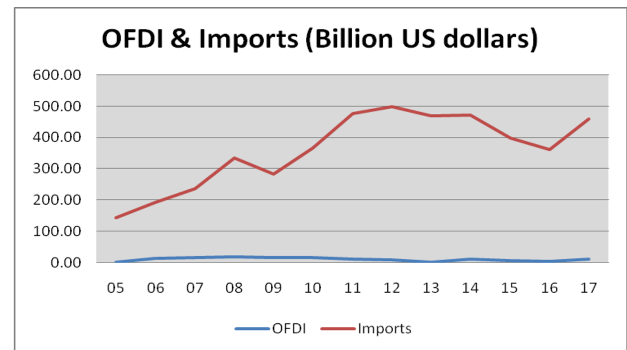


Source: Data compiled from OECD, UNCTAD and RBI

CASE 2: Correlation between ODI and Imports:

Here, the overseas direct investments were considered as X and imports were considered as Y. The correlation coefficient (r) for the data set was -0.202, and the coefficient of determination (r^2) was 4.08%. This signifies that both the variables considered, i.e. ODI and Imports, are uncorrelated. Since the value of r is almost nearing zero, both the variables considered have no relationship with each other. Change in one does not impact the other in any way. Coefficient of determination also reveals that only a meager 4.08% variation in imports can be credited to the relationship with ODI values.

Figure 4: Overseas Direct Investments & Imports



Source: Data compiled from OECD, UNCTAD and RBI

CASE 3: Correlation between ODI and GDP:

Here, the overseas direct investments were considered as X and GDP was considered as Y. The correlation coefficient (r) for the data set was 0.060, and the coefficient of determination (r^2) was 0.36%. Observing the values it can be safely concluded that ODI and GDP have zero correlation. There is no relationship between the two variables. Any change in ODI doesn't have any significant impact on the GDP of the country.

The detailed results for the analysis are presented in Table 2.

Table 2: Statistics showing data analysis performed

Test Conducted for OFDI	Results generated for		
	Exports	Imports	GDP
r	-0.323	-0.202	0.060
r2	10.43%	4.08%	0.36%

V. THE ECONOMIC IMPACT OF OVERSEAS DIRECT INVESTMENT

Balance of Payments Manual: Fifth Edition (BPM5) (Washington, D.C., International Monetary Fund, 1993) FDI refers to an investment made to acquire lasting interest in enterprises operating outside of the economy of the investor. According to Organization for Economic Co-operation and Development (OECD), an investment of 10% or above from overseas is considered as FDI. In India, foreign direct investment policy is regulated under the Foreign Exchange Management Act, 2000 governed by the Reserve Bank of India.

According to the RBI, "Foreign Direct Investment (FDI) is the investment through capital instruments by a person resident outside India (a) in an unlisted Indian company; or (b) in 10 percent or more of the post issue paid-up equity capital on a fully diluted basis of a listed Indian company", and "Foreign Portfolio Investment is any investment made by a person resident outside India in capital instruments where such investment is (a) less than 10 percent of the post issue paid-up equity capital on a fully diluted basis of a listed Indian company or (b) less than 10 percent of the paid up value of each series of capital instruments of a listed Indian company". The FDI in India can be observed by examining the statistics for inward as well as outward

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flow of funds in and from the country. Table 3 shows the value of FDI inflows and outflows in India for a time span of 13 years from 2005 to 2017.

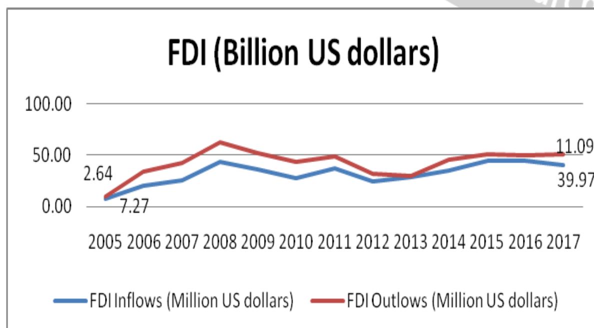
Table 3: FDI Inflows and Outflows in India

Year	FDI Inflows (Billion Us Dollars)	FDI Outflows (Billion Us Dollars)
2005	7.27	2.64
2006	20.03	14.04
2007	25.23	17.03
2008	43.41	19.26
2009	35.58	16.10
2010	27.40	15.97
2011	36.50	12.61
2012	24.00	8.55
2013	28.15	1.77
2014	34.58	11.69
2015	44.01	7.52
2016	44.46	5.05
2017	39.97	11.09

Source: Compiled from UNCTAD, OECD and RBI

Figure 5 shows the total FDI inflows and outflows in India for a span of 13 years from the year 2005 to 2017. It can be analyzed that both the inflows and the outflows has an upward trend till 2008, where FDI inflows had reached US$ 43.41 billion and FDI outflows were US$ 19.26 billion. But a declining trend is observed for the further years, where the inflows picked up by 2015 but the outflows have really not reached the limits as earlier. This can be adjoined to the fact that during that span of 2008 many economies were undergoing a financial crisis instigated in the United States. Even so the overall representation of the data portrays a positive change in the flow of FDI, both inflows as well as outflows.

Figure 5: Foreign Direct Investment Inflows and Outflows in India



Source: Data compiled from OECD, UNCTAD & RBI

Since this paper mainly focuses on the outward investments done by Indian companies, a detailed data analysis for Overseas Direct Investment (ODI) is undertaken. When it comes to ODI One can invest in India - either under Automatic Route, which does not require approval from RBI, or under Government Route, which requires prior approval from the concerned Ministries/Departments, via a single window, i.e. Foreign Investment Facilitation Portal (FIFB) (that is administered by the Department of Industrial Policy & Promotion (DIPP), Ministry of Commerce and Industry, Government of India). The routes under which foreign investment can be made according to RBI are the Automatic Route and the Approval Route and the details for adopting any of the mentioned routes can be enumerated as follows:

Table 4: Routes under which Foreign Investment can be made

Automatic Route	Approval Route
An Indian party does not require any prior consent from RBI	An Indian party is required to take prior approval of the Reserve Bank for which a specific application in FORM ODI with prescribed documents
An Indian party is required to approach the AD category – 1 bank	ODI not meeting conditions prescribed for automatic route
ODI investment within limit of 400% of Indian Party's Net Worth	Overseas investments by: Proprietorship concerns Unregistered partnership firms Registered Trusts/ Societies satisfying certain eligibility criteria
ODI by Indian Party engaged in financial services sector (subject to prescribed conditions)	Indian party undertaking financial commitment without equity contribution in JV/WOS
ODI in oil sector (subject to prescribed conditions)	

Source: RBI website

The Capital instruments permitted for receiving foreign investment in an Indian company include equity shares, debentures, preference shares and share warrants issued by the Indian company. The companies can either take up a Joint Venture (JV) or start a Wholly Owned Subsidiary (WOS). Joint Ventures means a foreign entity formed, registered or incorporated in accordance with the laws and regulations of the host country in which the Indian party makes a direct investment. Wholly Owned Subsidiary means a foreign entity formed, registered or incorporated in accordance with the laws and regulations of the host country, whose entire capital is held by the Indian party.

The statistics analyzed for ODI by India highlight the fact that there were many investments done by corporate overseas during the span of three to four years, 2006 to 2009, that reached to US$ 19 billion. But, later on it is observed that the average ODI for the subsequent time span highlights a poor performance and reduction in the overseas investments that reached lowest during the year 2013 to only US$1.77 billion. The average FDI inflows during the last decade were observed to be US$ 31.58 billion, whereas the outflows averaged to US$ 11.02

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billion. It is prominently observed that the outflows of FDI over the years are showing a declining trend.

VI. CONCLUSION

Overseas Direct Investment proves to be a very attractive form of entry into the global market place. And the overall statistics of the world portrays India as an upcoming hub for attracting foreign direct investment. The overall picture of the Indian investment abroad looks a little poor when the recent decade of statistics are considered. Even so the contribution of OFDI in building the nation cannot be overlooked. The research has proved that ODI does not have direct relationships between any of the economic factors, i.e. exports, imports and GDP. It is one of the avenues that the country's MNCs can peruse as an expansion tool for capturing the overseas market. Naturally, the revenue that the ODI generates for the country cannot be ignored. Having ODIs are important in the country as they help Indian companies to expand and generate more revenue for the Indian parent company. ODIs are also important drivers of foreign trade through increased exports of plant & machinery and goods & services from India and also a source of foreign exchange earnings by way of dividend earnings, royalty, technical know-how fee and other entitlements on such investments (or financial commitment). Thus, Indian government should take more initiatives to encourage Indian multinationals towards Greenfield investments and/or JV and WOS for expansion of their business activities.

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