FOREIGN INVESTMENT AND ITS IMPACT ON INDIA'S FOREIGN TRADE: AN ECONOMIC ANALYSIS

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Abstract

India is rich in natural resources and but poor in investment. This is the general trend. This trend leads to low economic development. Moreover, in order to remove poverty and unemployment India needs more capital. However the domestic supply of capital is lesser than the demand for capital for greater level of economic growth. Here foreign investment assumes importance and it is also necessary to use it effectively and efficiently for higher growth rate. This study tries to investigate the impact of foreign direct investment on foreign trade in India and further attempt to suggest policies for effective use of foreign direct investment for foreign trade as well as economic development.This analytical study is taking Foreign Direct Investment and Foreign Trade like exports and imports and Gross Domestic Products. This study reveals that to find out the causal relationship between various trade variables such as GDP, export and import and FDI, regression analysis analysis is used and the results shows that FDI and GDP and exports has greater relationship. This means FDI causes increase in GDP and India's exports. But the India's foreign imports are not influenced by the FDI.

Key Words: Foreign Direct Investment. GDP, Exports and Imports.

Introduction

Foreign trade plays an important role in the development of any country. Trade can be considered a social activity because it provides goods and services to satisfy the human wants. Each country has to buy the goods and services, which it requires, but cannot produce from the other countries and similarly sell the excess produce goods to other countries. This process of buying required goods and services from the other countries and selling of surplus goods and services to other countries is known as foreign trade. Foreign Investment comprises foreign direct investment (FDI) and foreign portfolio investment (FPI). The two categories are conceptually distinct in several respects. FDI represents a long-term vision and strategic commitment of the investors to the recipient economy.

In contrast, FPI is intrinsically short-term aiming to maximize risk-return payoffs from capital markets. While both FDI and FPI are reflected in capital structures of resident enterprises as equity held by non-resident entities, FDI is distinguished by the investor's desire to hold a controlling stake in the enterprise. In this respect, foreign investment policies of host economies usually refer to FDI policies with operational procedures for portfolio investment being functionally inclusive aspects of such policies. Foreign investment refers to the investment in domestic companies and assets of another country by a foreign investor. Foreign indirect investment involves corporations, financial institutions, and private investors that purchase shares in foreign companies that trade on a foreign stock exchange. This analytical study is taking Foreign Direct Investment and Foreign Trade like exports and imports and Gross Domestic Products.

Review of Literature

Chandrama Goswami et al., (2012) in their study reveals that after pursuing an inward looking policy of import substitution with public regulation in charge for more than four decades, India has adopted the New Economic Policy (NEP) in 1991 in the wake of economic crisis. The NEP has removed all sorts of biases against exports initiating reforms in the areas of international trade, investment, financial sector, and industrial and public sector deregulations. The flows of foreign capital are being welcomed. The East Asian experience has shown that the export-led growth strategies have been facilitated by FDI transferring into the host country technology, managerial and other expertise needed to exploit the country's comparative advantage. Against this back-drop, this study has three fold objectives. First, it investigates the trends of FDI in India during the period 1991-92--- 2010-11. Second, based on the yearly time series data, the relationship between FDI & manufactured exports has been examined for the same period by using the vector error correction model (VECM).The study found bi-directional causality between FDI and exports. Finally, the paper depicts the present status of FDI & exports in North East Region (NER) with a focus on their prospect. The Look East Policy (LEP) of the govt. may benefit the region because of its strategic location. However, despite having natural advantage of trade with neighbouring countries and the potentiality to develop various industries as being endowed with vast natural resources, the NER fails to attract any sizeable amount of FDI due to infrastructural and other bottlenecks. The need is to remove such fundamental constraints through strategic intervention

Shib Sankar Jana et al., (2020) in their papers reveals that the study seeks to foster fresh empirical evidence on how FDI is relevant to the foreign trade growth in India under a time-varying parameter model with vector autoregressive specification. The Johansen's cointegration test documents a significant and positive long-run co-movement between FDI and foreign trade in India. The vector error correction model suggests a unidirectional long-run causality from foreign trade to FDI. However, the Granger causality test confirms a bidirectional short-run causal relationship between these variables. Further, the variance decomposition analysis approves strong exogeneity of foreign trade. Again, the impulse response function analysis reveals that the responses generated from a positive shock of foreign trade to FDI and vice versa are small and initially negative and thereafter remain persistently positive at a constant level. The study finally concludes that the absence of long-run causality from FDI to export is the result of much domestic market orientation of foreign investors and less emphasis on the export-oriented sectors in India.

Statement of Problem

India is rich in natural resources and but poor in investment. This is the general trend. This trend

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leads to low economic development. Moreover, in order to remove poverty and unemployment India needs more capital. However the domestic supply of capital is lesser than the demand for capital for greater level of economic growth. Here foreign investment assumes importance and it is also necessary to use it effectively and efficiently for higher growth rate. This study tries to investigate the impact of foreign direct investment on foreign trade in India and further attempt to suggest policies for effective use of foreign direct investment for foreign trade as well as economic development.

Objectives of the Study

The specific objectives of the study are:

1. to discuss the importance of foreign direct investment, export and imports in India
2. to analyze the impact of foreign direct investment in GDP and foreign trade; and
3. to suggest policies.

Methodology

The present study uses secondary data relating to GDP, FDI, exports and imports, of India. The data have been collected from 2000-01 to 2020-21 from the publication of websites, Economic Survey, RBI bulletin and many other governmental organizations. Various statistical tools like multiple regression analysis is used this present study.

Results and Discussion

Foreign Total Investment Flows in India

Table 1 explains the foreign direct investment and foreign portfolio investment for the year 2000-01 to 2020-21. Table 1 reveals that the FDI investment in equity increased significantly since 2000-01 to 2020-21. During 2011-12, FDIs and FII are reduced. The FDI investment in equity during 2020-21 was Rs.3,09,867 crore the highest even in a single year.

Table:1– Foreign Investment and Foreign Trade Variables

Year	GDP	FDI	Exports	Imports
2000-01	1864773	18406	44560.3	50536.5
2001-02	1972912	29235	43826.7	51413.3
2002-03	2047733	24367	52719.4	61412.1
2003-04	2222591	19860	63842.6	78149.1
2004-05	2389660	27188	83535.9	111517.4
2005-06	2604532	34188	103090.5	149165.7
2006-07	2848157	88446	126414	185735
2007-08	3893457	66791	162904	251439
2008-09	4158676	180788	185295	303696
2009-10	4507637	190645	845534	1363736
2010-11	4885954	157819	1142649	1683467
2011-12	8736039	154961	1465959	2345463
2012-13	9215125	146954	1634318	2669162
2013-14	9817822	186830	1905011	2715434
2014-15	10522686	215893	1896445	2737087

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2015-16	11357529	294258	1716378	2490298
2016-17	12165481	283292	1854096	2566820
2017-18	12034171	288889	1956515	3001033
2018-19	12744203	309867	2307726	3594675
2019-20	13271471	353558	2219854	3360954
2020-21	12453430	442569	2154339	2909937
AAGR	**0.10**	**0.24**	**0.30**	**0.31**
CGR	**0.124**	**0.175**	**0.270**	**0.283**

Source: Reserve Bank of India Bulletin, 2000-01 to 2020-21.

The average annual growth rate is 0.10 per cent, 0.24 per cent, 0.30 per cent and 0.31 per cent for GDP, FDI, Exports and imports respectively. The compound growth rate for GDP, FDI, Exports and imports are 0.124, 0.175, 0.270 and 0.283 per cent respectively.

Foreign Investment and Foreign Trade

The present study carries out the multiple regression analysis for estimating how far foreign direct investment determines the GDP, exports and imports. For this purpose the researcher collected the secondary data from 'Reserve Bank of India Bulletin' for 21 years period from 2000-01 to 2020-21.

Foreign Direct Investment and Exports

To identify the major variable influencing the exports in India, Regression analysis has been applied by keeping foreign direct investment as independent variables and exports as dependent variable. The estimated values are presented in Table 2.

Table: 2 - Multiple Regression Analysis - Foreign Direct Investment and Exports

Model Summary

R	R Square	Adjusted R Square	Std. Error of the Estimate
0.886	0.786	0.774	4.2966

a.Predictors: (Constant), FDI

ANOVA

	Sum of Squares	**df**	**Mean Square**	**F**	**Sig.**
Regression	1.28E+13	1	1.28E+13	69.598	0.000
Residual	3.5E+12	19	1.84E+11		
Total	1.63E+13	20			

a. Predictors: (Constant), FDI

b. Dependent Variable: Exports

Coefficients

	Unstandardized Coefficients		**Standardized Coefficients**	**t**	**Sig.**
	B	Std. Error	Beta		

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(Constant)	-18987.235	158295.278		-0.120	0.906
FDI	6.363	0.763	0.886	8.343	0.000

a. Dependent Variable: Exports

The multiple regression result reveals that it has been found that the dependent variable, namely India's export is positive relationship and significant with a high R^2 value of 0.786 and also it has a significant The constant value is negatively related to dependent variable. 'F' value of 69.958. The 't' value is found significant at 5 per cent level and the 't' value 8.343 is positively related. It implies that one unit increase in this variable FDI other things remaining constant, it may lead to an increase of export 6.363 unit. Although 't' values are significant, the R^2 is very high. This model said to explain the foreign direct investment influenced by the India's total exports.

Foreign Direct Investment and Imports

To identify another major variable influencing the total import in India, another regression analysis has been applied by keeping foreign direct investment as independent variable. The dependent variable India's total import is included. The model has been found with high R^2 value 0.752 and the variable India's import have also significant regression coefficient. The intercept term and coefficient of 't' are positively significant at 5 per cent level. The 'F' value57.624 of the model states that the model has overall significance at 5 per cent level.

Table: 3 - Multiple Regression Analysis - Foreign Direct Investment and Imports

Model Summary

R	R Square	Adjusted R Square	Std. Error of the Estimate
0.867	0.752	0.739	6.8588

a.Predictors: (Constant), FDI

ANOVA

	Sum of Squares	**df**	**Mean Square**	**F**	**Sig.**
Regression	2.711E+13	1	2.711E+13	57.624	0.000
Residual	8.9385E+12	19	4.704E+11		
Total	3.605E+13	20			

a. Predictors: (Constant), FDI
b. Dependent Variable: Imports

Coefficients

	Unstandardized Coefficients		**Standardized Coefficients**	**t**	**Sig.**
	B	Std. Error	Beta		
(Constant)	6882.425	253101.158		0.027	0.979
FDI	9.257	1.219	0.867	7.591	0.000

a. Dependent Variable: Imports

The 't' value is found significant at 5 per cent level and the 't' value 7.591 is positively related. It implies that one unit increase in this variable FDI other things remaining constant; it may lead to an increase of imports 9.257 unit. This model said to explain the foreign direct investment influenced by the India's total imports.

Relationship between GDP, FDI and Foreign Trade

The major determining factor affecting the FDI, India's exports and imports in India are analysed through regression analysis. The main factor GDP, India's export and imports and FDI will be considered. The estimated values are presented in Table 4.

Table: 4 - Multiple Regression Analysis - Foreign Direct Investment and GDP, India's Exports and Imports

Model Summary

R	R Square	Adjusted R Square	Std. Error of the Estimate
0.981	0.962	0.956	9.2570

a. Predictors: (Constant), FDI, Exports, Imports

ANOVA

	Sum of Squares	**df**	**Mean Square**	**F**	**Sig.**
Regression	3.719E+14	3	1.240E+14	144.671	0.000
Residual	1457E+13	17	8.569E+11		
Total	3.865E+14	20			

a.Predictors: (Constant), FDI, Export, Import

b. Dependent Variable: GDP

Coefficients

	Unstandardized Coefficients		**Standardized Coefficients**	**t**	**Sig.**
	B	Std. Error	Beta		
(Constant)	1674185.534	348683.686		4.801	0.000
FDI	7.694	3.844	0.220	2.002	0.002
Exports	3.596	3.009	0.739	1.195	0.004
Imports	0.139	1.882	0.042	0.074	0.942

a. Dependent Variable: GDP

After estimating the regression, it has been found that the dependent variable, namely GDP is positive relationship and significant with a high R^2 value of 0.962 and also it has a significant 'F' value of 144.671. The 't' value is found significant at 5 per cent level in the variable FDI (2.002) and Export (1.195) It implies that one unit increase in this variable FDI and exports the other things remaining constant; it may lead to an increase of FDI is 7.694 units and exports is 3.596 units. But the 't' value of imports 0.074 is not significant. This model said to explain the GDP influenced by the variables like FDI

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and India's export. Hence, it is suggested that suitable policies may be formulated as regards the development of FDI it will leads to increase the GDP and export in India.

Conclusion

To find out the causal relationship between various trade variables such as GDP, export and import and FDI, regression analysis analysis is used and the results shows that FDI and GDP and exports has greater relationship. This means FDI causes increase in GDP and India's exports. But the India's foreign imports are not influenced by the FDI. Thus the foreign direct investment highly advantages for the foreign trade of India. However, it has to be very careful while allowing foreign direct investment and therefore necessary policy measures have to be initiated especially to generate more employment opportunities and create adequate and attractive infrastructural facilities through effectively using foreign investment.

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