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Call: 08813907089 | E-mail ID: ijraset@gmail.com

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Foreign Direct Investment

Aishwarya Raul

I. INTRODUCTION

A. Foreign Direct Investment

Is an investment in the form of ownership in a business in one country by a company based in another country.
It is thus distinguished from a foreign portfolio investment by a notion of direct control.
Foreign direct investment includes "mergers" and "acquisitions", building new facilities, reinvesting profits earned from overseas operations and intra company loans. It refers to a lasting management interest (10 percent or more of voting stock) in a company operating in an economy other than that of the investor.

II. FACTORS AFFECTING FDI

FDI is more conducive in the long-term growth and development than other forms of capital inflow. FDI brings with it foreign technology and management skills. Fast growing economies absorb more FDI. FDI flows into countries with relatively stable economic conditions.
Countries want to attract FDI into the primary sector like petroleum, mining and agriculture for revenue purposes. Investment in the secondary and tertiary sectors bring jobs to absorb labour from lower productivity sectors which is important for emerging markets where agricultural jobs are important.
The factors that attract FDI to rich countries may not be the same as factors that attract FDI to poor countries.
Some may trade off more educated labour in exchange for lower wages or access to a lucrative but protected market. FDI flows are less volatile that other capital flows. FDI helps in access to resources and markets, efficiency gains and acquisition of strategic assets.
The relationship of FDI with several macroeconomic variables like the size and growth potential of the host market, economic stability, the degree of openness of the host economy and income level, the quality of institution and level of development.
Large host countries attract more FDI. A weak real exchange rate may also increase FDI as firms take advantage of the low prices of the host markets to purchase facilities and to increase profits on goods. Clustering effect is the gathering together of foreign firms either due to linkages among projects or due to herding.
Institutional quality is a likely determinant of FDI. Good governance is associated with higher economic growth which attracts more FDI.
Poor institutions with problems like corruptions add to investment value.
The other thing is, secondary sector FDI flows are drawn both to advanced and emerging economies under similar macroeconomic circumstances. Labour market FDI flows more into emerging markets.

III. MAJOR DETERMINANTS OF FDI

A. Geographical location
B. Population
C. History
D. Economic Resources
E. Ideology
F. Efficiency of Government and Nature of Political Leadership
G. Quality of Diplomacy

IV. FOREIGN PORTFOLIO INVESTMENT

Foreign Portfolio investment (FPI) is the addition of international assets to the portfolio of a company. It is a form of portfolio diversification, achieved by purchasing stocks or bonds of a foreign company. Both FPI and FPI are encouraged in emerging nations. FDI involves greater responsibility to meet the regulations of the host country.

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V. ADVANTAGES OF FDI

A. FDI creates and maintains economic growth in the recipient country and the country making the investment.
B. Developing countries have encouraged FDI as a means of financing construction of new infrastructure and creation of jobs for local workers.
C. Multinational companies benefit from FDI as it helps expanding into international markets.
D. Increases Employment and Economic Growth: FDI boosts manufacturing and services sector. Skilled as well as unskilled labour finds work. Increased employment increases income and enhances buying power. Thus, the economy of the country improves.
E. Human Resource Development: Human Capital refers to the knowledge and competence of workforce. Skills gained and enhanced through training and experience boost the education and human capital quotient of the country. Once developed, human capital is mobile. It can train human resources in other companies and create a ripple effect.
F. Development of backward areas: FDI ensures this when factories are built, offices are built and the areas around it are developed.
G. Provision of Finance & Technology: Recipient businesses get access to latest financing tools, technologies and operational practices from across the world. Over time, the introduction of newer technologies and processes results in their diffusion into the local economy, resulting in enhanced efficiency and effectiveness of the industry.
H. Increase in exports: Not all goods produced through FDI are meant for domestic consumption. Many products are exported. The creation of 100% Export Oriented Units and Economic Zones have further assisted FDI investors in boosting their exports.
I. Exchange Rate Stability: The constant flow of FDI into a country translates into a continuous flow of foreign exchange. This helps the country's Central Bank maintain a comfortable reserve of foreign exchange. This in turn ensures stable exchange rates.
J. Inflow of capital is beneficial for countries with limited domestic resources, as well as for nations with restricted opportunities to raise funds in global capital markets.
K. Creation of a Competitive market: By facilitating the entry of foreign organisations into domestic marketplace, FDI helps create a competitive environment and breaks domestic monopolies. This fosters innovation.

VI. DISADVANTAGES OF FDI

It involves regulation and oversight of multiple governments, leading to high political risk.

1) Disappearance of cottage and small-scale industries
2) Contribution to pollution
3) Exchange crisis
4) Cultural erosion
5) Political corruption
6) Inflation in economy
7) Trade Deficit
8) World bank and IMF aid

VII. FDI IN INDIA

India receives one of the largest FDI in the world. The top investor countries in India are: Singapore, US, Canada, UK, China, Mauritius.

The top FDI recipient sectors in India: pharmaceuticals, automobile, electrical equipment. Sectors that showed the steepest decline are telecommunications, hotel and tourism. The state that received the highest FDI was Gujrat, Maharashtra, Karnataka, Delhi and Tamil Nadu.Two Indian cities – Bengaluru and Delhi are considered world's most favourable ecosystems to build globally successful start-ups. India has announced the ambitious National Infrastructure Pipeline (NIP) covering both economic and social infrastructure projects. This is to provide world class infrastructure across the country with energy, roads, railways and urban development projects as major beneficiaries. FDI policy initiatives and relaxations have been announced in multiple sectors like defence, public sector undertakings like oil refineries, telecom, power exchanges, insurance and stock exchange. A robust FDI policy is also in place. Key reforms include implementation of Goods and Services Tax (GST) to establish single market, introduction of Insolvency and Bankruptcy code in 2016 and consolidation of labour laws under 4 major codes (wages, industrial relations, social security and occupational safety, health and working conditions).

The Government also introduced PLI schemes in 13 flagship sectors.

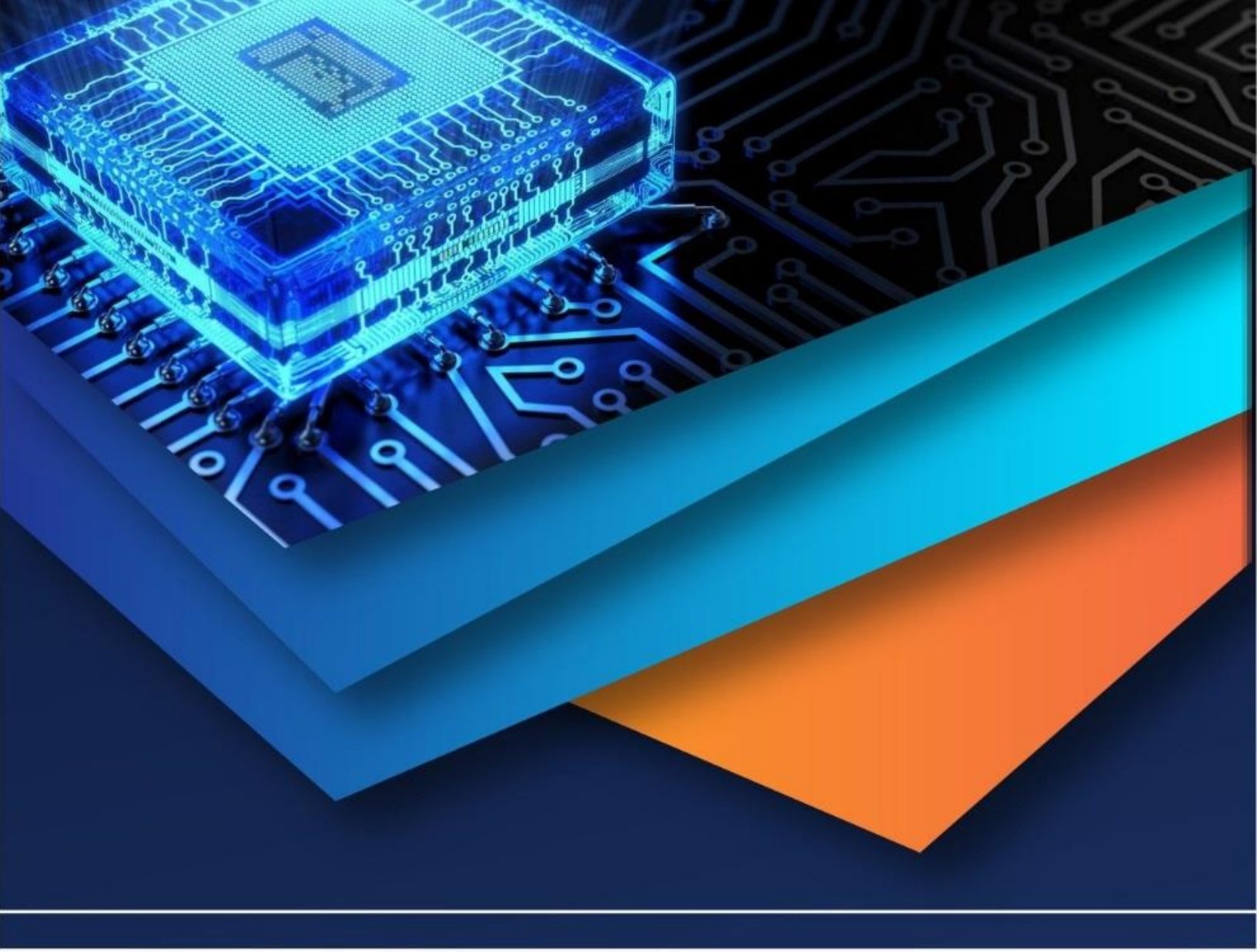
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VIII. TRENDS IN GLOBAL FDI

Country with highest FDI: Japan
Top 5 countries for FDI are UK, USA, India and Germany.
Biggest investors in the world are European Union, Netherlands, United States, United Kingdom.

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