Role of Foreign Direct Investments (FDI) in Service Sector in India

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Abstract

Service Sector is the lifeline for economic growth of a country. Service sector has emerged as the most dynamic sector of Indian economy particularly from last one and a half decade and this sector is contributing significantly to GDP, employment and structural transformations. Foreign direct investment has been instrumental behind the growth of service sector in India. The present paper focuses on the financial year-wise analysis of FDI equity inflows and to know the sectors attracting highest FDI equity inflows in India over the period of 2004-05 to 2014-15. The secondary data has been used for study. The analysis has revealed that service sector attracts the highest amount of FDI inflows into India. DDTA (Double taxation avoidance agreement) between India and Mauritius helps in obtaining maximum FDI via Mauritius.

Keywords: Foreign Direct Investment, Service Sector, India

Introduction

India is a vast country and many sectors contribute to the country's GDP. Indian Economy is classified into three sectors: Primary, Secondary and Service Sector. The primary sector is an economic description concerned with the extraction of raw material. It includes farming, fisheries, forestry and animal husbandry etc. Secondary sector includes manufacturing industries. In service sector all types of services are included. They include trade, hotel & restaurants, transport, storage, communication, health care, education etc. The reason for growth of service sector is due to increase in urbanization, privatization and more demand for intermediate and final consumer services. The contribution of service sector has increased with pace because foreign investors have shown interest in investing into the country. This because India has a large pool of highly skilled, low cost and educated workers in the country. This shows a positive change in share of service sector in India's GDP. Foreign Direct Investment (FDI) means investment by non-resident entity/person resident outside India in the capital of the Indian company under Schedule 1 of FEMA Regulations 2000. FDI inflows into core sectors are assumed to play a vital role as a source of capital, management, and technology in countries of transition economies. It is a high level indicator of economic health of a country. The new policies have succeeded in enhancing foreign capital inflows in the Indian economy. With the volume of FDI inflows into India increasing significantly from Only US $ 97 million in 1990-91 to more than 60.1 billion in 2016-17. India has emerged as one of the leading FDI destinations among developing countries.Despite significant procedural relaxations and liberal policies, FDI inflows in India, though much higher than the past, has not been able to reach the levels of the ASEAN economies or China. FDI growth in important sector like services over all foreign inflow into the country increased 22% to $ 35.81 billion during year 2014-15. There has been a significant growth in FDI inflows in 2013-14 and 2014-15 (April-October) in general and in Services Sector in particular. In 2014-15 FDI inflows to service sector grew by a shopping 70.4 percent to 16.4 billion US $. The rising trend is continuing in the first seven months of 2014-2015 with the FDI equity inflows in the services sector growing by 74.7% to dollar 14.8 billion. It helps to establish new companies. All of these contribute to economic growth of the country.

Literature Review

Ahmad (2015) analyzes not only the impact of foreign direct investment on gross domestic product but also to analyze trend of foreign direct investment in India since liberalization. Further he concludes that it is the need of hour to adopt imperative and innovative policies and good corporate government practices at par with international standards, to attract more foreign direct investments. **Sood(2015)** analyzed the contribution of FDI for GDP growth. The study concluded that the association and dependence of GDP on FDI in India is found to be statistically significant whereas the relationship and dependence of investment by FII on total FDI in India is insignificant. **Singh (2015)** analyses contribution of service sector in GDP, employment, FDI and Export services. The paper found that the service sector faces a number of problems such as infrastructure facilities to poor, cost of service delivers is high and some more. **Arya and Ashwani (2014)** examine the impact of government expenditure in social sector on economic growth at state level for 15 major states. Impact of expenditure on social sector has no significant impact on growth. But it has an impact on human resource development and indirectly participates in economic development. **Akhtar(2013**)found and stated in his study on Inflows of FDI in India as Pre and Post Reform Period that during pre liberalization period FDI has increased at Compounded Annual Growth Rate of 19.05 % and during post liberalization period it has grown to 24.28 %.**Kumari (2013)** examines the present and future status of FDI in India. She has done her study in the period of 2000-2012 and tried to examine the equity inflow of FDI and FDI trend in India during these years with the help of regression analysis and correlation tests. The FDI trend analysis result shows the upward trend of FDI inflow in India, which clearly shows that FDI is going to flourish in the near future, thereby increasing the economic growth. **Mukherjee (2012)** analyses that service sector is fastest growing sector in India, contributing significantly to GDP, GDP growth, employment, trade and investment. Aggarwal, Singla and Aggarwal (2012) exhibited the sector-wise & year-wise analysis of FDI's in India, and ranked the sectors based upon highest FDI inflows. It has been found that Mauritius invested highest in India followed by Singapore, Japan, and USA and so on. It was also shown that there has been a tremendous increase in FDI inflow in India during the year 2000 to 2011.**Bohra (2011)** analyzes FDI to developing countries in the 1990s was the leading source of external financing and has become a key component of national development strategies for almost all the countries in the world.

Research Methodology

To achieve the objective of the study secondary data on Indian economy for the period 2004-05 to 2014-15 has been used. The data is obtained from governmental and non-governmental published and unpublished sources, various websites related to foreign direct investment, annual reports, various bulletins of Reserve Bank of India, World Investment reports and Economic Survey, Government of India.

Objectives of the Study

The main objectives of the study are:

1. To know the trend of FDI inflow in India.
2. To study the sectors attracting highest FDI equity inflows in India.

Table 1: Financial Year-Wise FDI Equity Inflows in India

Year	Amount In Crores	Amount In USD Million	% Growth
2004-05	10,064	3,219	47%
2005-06	14,653	3,219	72%
2006-07	56,390	12,492	125%
2007-08	98,642	24,575	97%
2008-09	1,42,829	31,396	28%
2009-10	1,23,120	25,834	(-)18%
2010-11	97,320	21,383	(-)17%
2011-12	1,65,146	35,121	64%
2012-13	1,21,907	22,424	(-)36%
2013-14	1,47,518	24299	8%
2014-15	1,89,107	30931	27%

Source: As per DIPP's FDI data base

Analysis and Interpretations

FDI is an investment made by an entity in one country in an Industrial / business activity in another country. FDI becomes more vibrant in India after the introduction of new economic policy 1991. After liberal policies regarding Foreign Direct Investments in 1991, the amount of FDI received by India increased sharply. India attracts many Multi-national enterprises due to lower labour costs and high economic growth.

To achieve the objectives of this study an analysis on the basis of collected data is done. The result on the basis of secondary data are as follows:

From Table 1 it is analysed that total FDI equity inflow in India from different sectors during the year 2000-01 was US$ 2378.68 millions. It increases to 2704.34 million but decreased to US$ 2187.71 million in 2003-04. FDI inflows increases rapidly in year 2006-07 i.e. US$ 1249.77 million in this year. The reason behind this fast growth is change in policies regarding to retailing in India as Government gives approval for 100% for cash and wholesale trading and 51% for single branch retailing. In year 2009-10 and 2010-11 it started to dip by 18% and 19%. Again FDI inflows started to gain its momentum and foreign direct investment have been on rise in India. There was a growth of total FDI equity inflow of 27.29% during 2014-15 over 2013-14 in India.

It shows that Mauritius and Singapore on the top among the chart of 10 top investing countries into India followed by USA, Cyprus and Japan.

Table 2: Foreign Direct Investment flow to India: Country wise

Source Country Total FDI	2010-11 14,939	2011-12 23,473	2012-13 18,286	2013-14 16,054	2014-15 24,748
Mauritius	5,616	8,142	8,059	3,695	5,878
Singapore	1,540	3,306	1,605	4,415	5,137
U.S.A.	1,071	994	478	617	1,981
Cyprus	571	1,568	415	546	737
Japan	1,256	2,089	1,340	1,795	2,019
Netherlands	1,417	1,289	1,700	1,157	2,154
UK	538	2,760	1,022	111	1,891
Germany	163	368	467	650	942
UAE	188	346	173	239	327
France	486	589	547	229	347
Switzerland	133	211	268	356	292
Hongkong	209	262	66	85	325
Spain	183	251	348	181	401
China	2	73	148	121	505
Malaysia	40	18	238	113	209
South Korea	136	226	224	189	138
Luxembourg	248	89	34	539	204
Others	1,142	892	1,154	1,015	1,250

Source: www.rbi.org.in

According to Table III, Service sector attracts the highest FDI inflows with 20% of the total inflows followed by construction development 12%, Telecommunication 7% and computer software and hardware 6% respectively.

Conclusion

FDI plays an important role in economic development of India. It became possible due to the liberal policies and regulations regarding foreign direct investments through Government route and automatic route.

Table 3 : Sectors Attracting Highest FDI Equity Inflows in India

Ranks	Sector	2010-11 (April-March)	2011-12 (April-March)	2012-13 (April-March)	Cumalative inflows	%age of total in-flows (in terms of US $
1.	Service Sector	15,504 (3,296)	15,236 (5,216)	25,367 (4,660)	1,71,345 (37,063)	20%
2.	Construction Development : Townships, Housing, Built-ing-Up Infrastructure	7,590 (1,663)	15,236 (3,141)	6,562 (1,206)	1,00,363 (21,954)	12%
3.	Telecommunications (Radio Paging, Cellular Mobile, Basic Telephone Services)	7,542 (1,665)	9,102 (1,997)	507 (93)	57,585 (12,645)	7%
4.	Computer Software & Hardware	3,551 (780)	3,804 (796)	2,382 (435)	52,500 (11,640)	6%
5.	Drugs & Pharmaceuticals	961 (209)	14,605 (3,232)	5,389 (1,008)	48,257 (10,202)	5%
6.	Chemicals (Other than fertilizers)	10,612 (2,354)	18,422 (4,041)	1,466 (268)	40,366 (8,857)	5%
7.	Power	5,796 (1,272)	7,678 (1,652)	2,871 (526)	36,085 (7,825)	4%
8.	Automobile Industry	5,864 (1,299)	4,347 (923)	4,916 (895)	35,702 (7,653)	4%
9.	Metallurgical Industries	5,023 (1,098)	8,348 (1,786)	7,439 (1,385)	34,375 (7,426)	4%
10.	Hotel & Tourism	1,405 (308)	4,754 (993)	17,401 (3,190)	32,884 (6,526)	4%

As India is in double taxation avoidance agreement (DDTA) with Mauritius, which helps in attracting maximum FDI from Mauritius. India received maximum foreign investments from Mauritius, Singapore and Japan which shows a positive impact on growth of GDP of India. It is also analysed that the service sector receives the highest amount of FDI inflows followed by telecommunications sector and construction sector during 2011 to 2014. Investors are taking keen interest in investing and showing their growing confidence in India Economy. In order to attract more and more FDI inflows in country policy makers need to ensure transparency and consistency in making the policies.

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