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FOREIGN DIRECT INVESTMENT IN INDIA

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ABSTRACT

The investment made by company in new manufacturing and /or marketing facilities in a foreign country is referred to as Foreign Direct Investment(FDI) Investment made by Enron in power plant in India is an example of FDI.The investment made by a company in a foreign country over a given period is called Flow of Foreign Direct Investment the total amount of investment made by a company in a foreign country up to a given time is called The stock of Foreign Direct Investment. Out flow of FDI is called Out flow of Foreign Direct Investment and inflow of FDI is called Inflow of Foreign Direct investment.

Growth of FDI

The flow foreign investment has been increasing during 1975 to 1995 . The FDI increased From US $25 billion in 1975 to US 4$315 billion in 1975.The reason for increase in FDI is due to the desire of many foreign companies to establish manufacturing facilities in foreign countries in spite of decline in trade tariffs and import quotas. The other reason is the significant development of globalisationthroughout the world countries

Changes in the source of FDI

USA has been the major source of FDI .During 1970s half of the out flow of FDI was held by USA .The second position was occupied by UK .By 1990 Japan occupied by UK 1990 occupied the first position followed by USA.

The Recipient of FDI

The host country for foreign investment is the recipient country and a home country is a source country for foreign direct investment .USA occupies the first place in terms of total FDIs and Singapore occupies the first place in terms of FDI per capita (US $ 13,650) during 1985-95.

The theory of Foreign Direct Investment

There are several theories of FDI. These theories are from three complementary perspectives. One set of the theories explains the reasons why firms directly invest in foreign countries when the other alternatives like exporting and licensing are available. Another set of theories explains why some firms of the same industry often undertake FDI and why investment flows only to certain locations. The third set explains the best of the remaining two theories in the form of a single explanation.

Why FDI when Other Means are Available?

Some firms establish the manufacturing, distribution and servicing facilities in foreign countries, when exporting and licensing strategic alternatives are available.

Exporting and licensing strategies are explained in detail in International Strategic Management. Companies produce goods at home and transport them to foreign countries for sale under exporting strategy. Firms grant the right to produce and sell the firm's products for a royalty fee to the foreign companies under licensing. However, both these strategies suffer from limitations.

Limitations of Exporting :- though the companies find it easy to export goods there are certain limitations of exporting. They are.

- High costs of transpiration, shipment and transshipment.
- High cost of tariffs and Other forms of trade barriers.
- Low value of weight products like soft drinks and cement can be produced at any place.

Similarly, some of the costlier goods can also be produced easily at any place.
It would be advantageous to the firms to produce such products in foreign countries rather than exporting.

Limitations of licensing :- Internationalization theory

Explains the advantages of FDI over licensing. According to this theory the limitations of licensing are:

- Under licensing, firms give away valuable technical know-how to the foreign collaborator who would turn into a potential competitor in the future.
- The licensor firm cannot have tight control over the licensee's manufacturing, marketing other strategies and profitability in foreign country.

- The firms with competitive advantage in products and technology only cango for licensing. It does mean that the firms with the competitive advantages in marketing, management etc. cannot go for licensing strategy.

Advantages of FDI

Most of the limitations of exporting and licensing are turned to be the advantages of licensing. The significant among them are:

- Trade barriers like tariffs and quotas can be overcome through FDI.
- Firm's competitive strengths like management and organization can be exported through FDI Only.
- FDI Creates employment opportunities in the host country.
- FDI enlarges business activity in the host country.

The Pattern of FDI

Firms in the same industry go for FDI to enter foreign markets. Further firms concentrate their investments in certain locations.

Firms follow their domestic competitors' investment pattern in foreign countries regarding their FDI.

Product Life Cycle

Raymond Vernon's product life cycle theory explains the pattern of FDI over time.
According to Vernon's the firms originally developed the product to establish manufacturing facilities to produce the product in foreign Countries.

Xerox Originally introduced photocopier in USA. It later spread the manufacturing facilities in Japan (Fuji-Xerox), Great Britain (Rank-Xerox) and India (Modi-Xerox).

According to Vernon, firms establish manufacturing facilities in foreign countries, when the product reaches maturity stage in the home country. They invest in low-cost countries when cost becomes a competitive edge.

Benefits to the Home Country

- Inflows of foreign currencies in the forms of divided, interest etc. Nissan's profits repatriated to Japan are from its FDI in UK. They helped Japan for positive balance of payments.

- FDI Increases export of machinery, equipment, technology etc. from the home country to the host country. This in turn enhances employment opportunities.

- The firms and other home country firms can learn skills form its exposure to the host country and transfer those skills to the industry in the home country.

Host Country Benefits

- **Resource-Transfer Effects: -**

The Resources which are scare in host country are transferred from the foreign country. These resource include foreign capital, technology machinery and equipment, management and organization. Transfer of these resource develop the host country develop the Indian Industry, infrastructure and service sectors.

- **Employment Effects:-**

The FDI contributes for the establishment of new industries and business directly and for the employment of existing economic activity. Further, FDI helps for the developing of ancillary industries. These developments invariably increase the employment opportunities for the people of the host country.

- **Balance-of-payments Effects: -**

Balance of payments position and foreign exchange resources are very crucial from the view point of external situation of a country. India faced severe July 1991. In fact this adverse position, forced the Indian Government to announce economic liberalizations in July 1991.

Disadvantages of FDI to Host Country

Though the FDI benefits the host country and also costs the host country. Its costs are in the form intensifying competition, negative effects on balance of payments and impact on national sovereignty and autonomy.

- **Intensifying Competition: -**

Foreign MNCs have more competitive abilities in view of their large size resource base and widespread operations than that of the domestic companies. Hence, They pose severe competition and threat to the domestic companies.

Negative Effects on the Balance of Payments:-

The Foreign companies affects the balance of the host country in two ways.

IMPLICATIONS OF FDI FOR BUSINESS

We can draw the following implications of FDI for business:

Location-specific advantages arguments indicates the flow of FDI in Order to take the advantage of mineral and other resource in foreign countries.

IF the costs of transportation are minimum, it would be preferable for the companies to export.

If the costs or transportations and trade barriers are significant, it would be preferable to go for FDI.

The firm can go for licensing if the know-how is not valuable.

If the company's skills and capabilities are not available for licensing, better the company go for FDI.

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