CHAPTER-VIII

CONCLUSION AND POLICY RECOMMENDATIONS

FDI inflows into India like other EMCs[1] increased expeditiously after 1991 as most of these economies including India undertook structural and economic reforms in order to make their economy a favourite destination for foreign investments. As a result of these efforts which included the reduction of restrictions on international capital inflows, removal of unwanted trade barriers, there was a surge in FDI inflows into these economies. This was led largely by mergers, acquisitions, reflecting the extensive privatisation of state owned assets in a number of emerging countries. Notwithstanding the outpouring of FDI in EMCs during 90s, most investors remain stressed due to the magnitude of risks related to investing in these countries. Most of the time the investors were apprehensive about the matters relating to the policy framework, the enforceability of mutual agreements and contracts. MNCs had a strong feeling that the legal frame work of these countries needs to be properly understood. It is in this context that the economic reforms pursued by these economies played a major role in the changing the investment climate. The 1990s witnessed a significant shift towards market seeking FDI in a number of countries in contrast to the traditional approach for labour abundant economies to be later used as a manufacturing base for exports. India also experienced an increase in FDI by MNCs in order to capture its growing domestic market. After witnessing the initial upsurge in FDI inflows, in the period that followed the 1991economic reforms, India witnessed the trend of ups and downs in FDI inflows as has been proved by the data of various years. The uncertainty of FDI inflows led to policy changes by the government time and again in order to make the country a hot spot of investment by foreigners. FDI inflows in India remained sluggish, after global economic recession in 2008-09, despite sound domestic economic performance ahead of global recovery. On the other EMEs in Asia and Latin America received large inflows during the same

[1]Emerging market economies: An emerging market economy is a nation's economy that is progressing towards becoming more advanced, by means of rapid growth and industrialization. These countries also experience an expanding role on the political frontier.

period. This raised concern in India in the wake of widening current account deficit beyond the so called recognised sustainable level of 3.0 percent of GDP. However, the comprehensive and continuous FDI policy reforms ranging from privatisation, deregulation of sectors to strong IPR[2] have helped India tide over the problem of lack lustre performance towards attracting FDI. India now enjoys a status of an attractive destination for investment amongst the MNCs of developed countries. In the current economic scenario FDI has assumed significance because it is considered to be the most stable component of capital flows needed to finance the current account deficit along with providing access to advanced technology, knowledge of production process and getting access to export markets.

Taking notice of India's FDI policy in comparison to other EMEs it is found that while India began, with a relatively restrictive approach towards foreign investment, later on however it started deregulating its policies and followed a more liberalised policy stance. Since the early 1990s it allowed wider access to different sectors of the economy, eased its policies related to starting up business, it improved its macroeconomic parameters and fundamental. It cannot be denied that these efforts at attracting inflows have been successful. The effects of all these investment friendly measures led to the growing size of FDI inflows. Amidst the prevailing global economic situation, investors are-evaluating their investments in EMCs in the light of falling profitability and greater perception of risks.

The study begins with an introduction to the subject-matter under consideration. The objectives for carrying out the present work are also mentioned. The hypothesis and the methodology of the study are also explained. The period for the present study is from 1991 till 2013, this long period of study helped to understand the trend of FDI inflows and its impact on economic growth of India.

In the second chapter review of literature pertaining to various areas has been done in order to ascertain whether FDI inflows could contribute to increasing the growth rate

[2] Intellectual Property Rights: These are the rights given to persons over the creations of their minds. They usually give the creator an exclusive right over the use of his/her creation for a certain period of time. Some IPRs are copyright, patents, and industrial design rights; and the rights that protect trademarks, trade dress, and trade secrets: all these cover music, literature, and other artistic works; discoveries and inventions ,etc

of the host economy by augmenting the capital stock as well as with infusion of new technology. It is widely acknowledged that MNEs, with their expertise and managerial skills and knowledge about prevailing international marketing conditions, are expected to improve the product and factor productivity as well as export performance of the host country firms by creating certain positive externalities known as ‘spillovers’. Studies are reviewed in order to provide the justification for the current study. The review has been conducted in three broad categories. In the first part, the effect of FDI inflows on economic growth of countries other than India has been reviewed, this is followed by similar studies in India. In the next section, a study of the effect of FDI on trade of other countries followed by similar studies in India has been done. Finally, the review of literature on the effects of FDI on R&D activities of a country on similar lines is presented. The survey of literature regarding the impacts of FDI on economic growth, trade domestic R&D, innovative capabilities and productivity in a developing country provides diverse views, as some of the studies have found positive impact of FDI inflows on growth, trade and local R&D capabilities, on the other hand other studies found that the entry of foreign firms is not without any negative effect or consequences. They argued that the presence of foreign firms can crowd out domestic firms due to excessive pressure of competition. It is thus evident that a large number of empirical evidences are mixed and inconclusive on these issues. This may be due to the differences in the type of data used, choice of country, time periods, selection of independent variables, sources of data selection and applied methodology. Further it was found that there is a lack of research on the effect of FDI inflows on automotive industry in India. As industry specific dynamics, alter the impact of FDI, and are expected to create varying effects, therefore it is vital to identify the impact of FDI in this sector.

While surveying literature most of the studies highlighted the importance of policies formulated by the host country over governnment as an important conduit for larger FDI inflows. It is this aspect that has been dealt with in the next chapter.

The third chapter provides description of FDI related policies of the government of India. In the recent past the policies towards FDI have acquired great importance. The government of various countries all over the world are continuously amending their

FDI related policies to remove the hurdles to FDI inflows and ensure that it is internationally competitive. Since this study also makes an attempt to analyse the effects of FDI in Automotive Industry, the frame work of policies pertaining to FDI in automotive sector has also been examined. In the first section of this chapter the FDI policy in general has been discussed. This section also includes evolution of the FDI policy in India followed by the post reform scenario pertaining to FDI in India. In the second section the overall policy related to the automotive sector of India , evolution of the FDI policy related to the automotive industry since independence in India and its influence on the automotive sector in different phases have been discussed. The ongoing FDI policy pertaining to automotive sector has been also been described. The government has already allowed 100 p.c. FDI in this sector through automatic route however government should now direct its policies towards FDI in intensifying R&D activities in order to attain fuel efficiency, safety measures and alternate fuel engines.

The fourth chapter describes about the profile of FDI and automotive sector of India. It was found that the pro FDI policy of the government that has been elaborated in the third chapter provided a thrust to FDI inflows in the country. FDI enjoys high priority in the list of government strategies of economic development. Consequently the relative importance of debt creating inflows comprising of external assistance, external commercial borrowings, short term credit, and non resident Indians deposits has declined over a period of three decades. After examining phase wise trends and patterns of FDI inflows in India since 1991 it is observed that FDI in India started slowly and later on picked up moderately till the middle of 2000s and thereafter picked up robustly, although it was far lesser than the initial expected potential and expectations. However the robust growth in FDI inflows after the mid of 2000 showcases the confidence of international investors and MNCs in India's growth potential. The profile of automotive industry in India provides an insight into the key areas of prospective investment in this sector which have not been explored so far. Thus automotive industry has immense potential of growth in the near future. Also this chapter draws attention of the government towards the states and sectors which could be prospective destination of FDI inflows in future.

In chapter five the effect of favourable FDI policy on FDI inflows into various sectors and consequently on economic growth has been tested empirically. As mentioned this study covers the period when results of the reconstruction of the economy have just started pouring in and the period when India began to be recognised as the favourite destination of FDI after China. The huge market size, availability of highly skilled human resources, sound economic policy, abundant and diversified natural resources are factors that enable India to attract FDI. It was found that even though there has been increased flow of FDI into the country during the post liberalization period, the global share of FDI inflows in India is very less compared to other developing countries and emerging markets. Lack of proper infrastructure, unstable government, uncertain political environment, high corporate tax rates and limited export processing zones are considered to be the major problems for low FDI into the country. Multi-regression analysis also shows that neither total FDI inflows into Indian economy nor FDI inflows in automotive sector show a significant favourable impact on the GDP of our country. Nevertheless FDI inflows in automotive sector show better influence on GDP growth rate of India in the presence of other explanatory variables. Thus the hypothesis is accepted that FDI inflows in automotive industry show better performance in comparison to overall FDI.

In chapter six we have found that the effects of FDI on trade in India as international Trade is also known to be an instrument of economic growth (Frankel and Romer). It is found that there is unprecedented growth of global FDI since 1990 around the world because of the profound institutional changes implemented by various EMEs due to the successive globalisation waves of the 1980s and 1990s. These changes had their impact on the BOP of the Indian economy as well as affecting its external trade and performance, widening current account deficits (CAD) and depletion of foreign exchange reserves. This had contributed to loss of investors' confidence, putting the external sector under severe financial stress in India. To find a way out of the growing crisis it was suffering from, India initiated economic reforms. Government removed the constraints and de-regulated many policies related to various sectors. The study found that the foreign direct investment in automotive sector contributed to reduce, India's current account deficit. Thus in line with the hypothesis that export intensity of automotive industry is better as compared to other FDI firms.

In the seventh chapter the effects of FDI on R&D (Research and Development) and productivity of firms in automotive sector and overall economy was examined. These are the crucial areas of a domestic economy which are influenced by the presence of foreign technology and knowhow in India. The three groups of firms that were used for this comparative study were all FDI firms, non FDI firms and automotive firms with FDI inflows. The result shows that in terms of profitability index growth, the performance of all FDI firms is negative. Automotive firms have better profitability compared to the other two groups of firms. Non FDI firms are better than all FDI firms in terms of profitability. One important aspect which was noted in the result was that the R&D intensity of non FDI firm is also quite impressive. The result of the analysis related to the R&D intensity shows that automotive firms are more R&D intensive as compared to FDI and non FDI firms. Thus supporting the hypothesis that R&D intensity of automotive firms is better than other FDI firms and firms which do not receive FDI.

From the above it can be summed up that integrated, continuous and comprehensive economic reforms in general and FDI policy related reforms in particular have contributed significantly to bring FDI into our economy. These reforms improved India’s status as one of the most favoured destination of investment by the foreign investors. India at present also enjoys the privilege of an impressive GDP growth rate ranging from 6.5 to 7.5%. Indian economy is now more integrated and liberal. India also has FTA with many neighbouring and BRICS and other group of countries like G-20 countries. This integration has no doubt helped India to initiate market seeking exports and attract more investors from developed countries. However, on the flip side this has also made our economy vulnerable to global economic turbulence and financial fluctuations. For instance the recent Greece crisis in 2015 and Global recession of 2008-09 brought their share of financial trouble for Indian economy.

8.1 POLICY IMPLICATION OF THE STUDY :

It is found that strong macroeconomic stability is a very important growth driver of the Indian economy. Internal market growth is very important for attracting MNCs helping them to avail opportunities of achieving the scope of higher scale of production, which in turn could be sold in the domestic market and the surplus could be exported. Thus the policy makers should target to curb the inflationary pressures of the economy and cut down transaction costs as a strategy to attract more FDI.

Removing bureaucratic hurdles should be given top priority. Many MNCs rate India poorly in terms of ease of doing business in India. This calls for measures to check unnecessary restrictions and formalities. Priority should be accorded to good governance which comprises areas like efficient rule of the law, creating a quality internal business environment that fosters healthy competition for both indigenous and foreign subsidiaries. Political stability along with strong macroeconomic stability helps to draw more FDI. In fact India desperately needs to overhaul the entire gamut of policies related to efficient and effective administrative system. This requires strict implementation of the policies.

Government should increase the number of SEZs and EPZs so that MNCs can explore the possibilities of increasing the scale of production. This will ensure the availability of infrastructure and basic facilities development of communication, transportation facilities, good roads and railways connectivity. Thus the government needs to increase the number of infrastructural projects and do proper maintenance of the existing ones. This in turn will ensure increased inflows of FDI in the long run.

Automotive industry sustains enormous scope in the field of alternate fuel engine cars apart from petrol and diesel engines. This initiative calls for large chunk of funds that need to be allocated for research and development and innovation. Hence government should either subsidise the R&D efforts of the local firms or encourage foreign firms to undertake research and development in these areas. Also cost effective metals should be encouraged for making the body structure. Accordingly policy planners need to act in this regard.

To encourage phase/stage wise production activities or vertical FDI[3] the tariff and non tariff barriers should be reduced and some of these even removed. This will increase the efficiency of the MNCs to supply goods and services worldwide .

[3]Under this manufacturing procedure is subdivided into different stages, locating each stage in a country which is able to provide better and cost efficient opportunities of manufacturing that particular stage , later different stages of production is coordinated and merged .later on the final product is sold. This increases the efficiency and profitability of both MNCs and host countries.

There is lack of sector based FDI, this draws the attention of the government to decide the sector specific determinants of FDI and work on those factors to make them more effective to attract FDI. Government should give more importance to sector specific policies to attract FDI into a particular sector that holds the opportunities to create employment. This calls for indentifying those prospective sectors which have been unable to attract FDI inflows. The government need to provide lucrative incentives to attract FDI in these sectors.

The government also need to focus on the development of strong labour market rules and regulations that include effective minimum wages, procedures related to hiring and firing, safety of labour at work place, these measures will reduce the operating cost in the long run and enhance the procedures of settling disputed between both the parties.

8.2 LIMITATIONS OF THE STUDY :

The main limitation of the study is the non availability of continuous and comprehensive sector specific data related to automotive sector in India. It was really a tedious task to compile data published in the various issues of RBI bulletin and data published by CMIE.

The data published by WDI are in current US$, conversion of these data to local currency units becomes a difficult exercise in the absence of exchange rates for different years, especially for the time period before 1980s.

The study has not detailed the factors responsible for determining the inflows of FDI into automotive sector. The detailing would have given an insight into the growth drivers of the automotive sector in India.