

# Economic and Policy Determinants of Foreign Direct Investment: An Empirical Analysis in Context of India

Ms Mohita Maggon

## ABSTRACT

*India is identified as one of the most attractive long-term investment destinations. The presence of large domestic market, fairly well developed financial architecture and skilled human resources, it can attract much larger foreign investments than it has done in the past. India's present international investment regime facilitates easy entry of foreign capital in almost all areas subject to specific limits on foreign ownership. Entry options have not only become procedurally simpler, but prospects for higher yields from investment have also become brighter. But further boost to Foreign Direct Investment (FDI) will depend significantly on further liberalization of its foreign investment regime. The paper provides the brief synthesis of the regime and analyzes the economic and policy variables as the important determinants of FDI inflows to India. It also emphasizes the areas where the policy needs to be reviewed and to be made more conducive for foreign investment.*

**Key Words:** Foreign Direct Investment (FDI), Foreign Portfolio Investment (FPI), Gross Domestic Product (GDP), Openness.

## I. INTRODUCTION

India is the largest democracy and fourth largest economy in terms GDP in the world. With its consistent growth performance and high-skilled manpower, India provides enormous opportunities for foreign investment. Since the beginning of economic reforms in 1991, major reform initiatives have been taken up in the field of investment, trade and financial sector. Enactment of Competition Act, liberalization of Foreign Exchange Management Act (FEMA), and amendments in Intellectual Property Right laws and many other initiatives make India attractive for business. India is the second most attractive foreign Direct Investment destination (A.T. Kearney 2007). Also it is the second most attractive destination among transnational Corporations for FDI 2007-09 (UNCTAD's World Investment Report, 2007).

Though FDI inflows have responded positively to policy changes by increasing from US\$ 165 million in 1990-1991 to US\$ 90 billion in 2008-2009, there might have been much more had foreign investment not been regulated in some key areas. Till the 1990s,

the policy was heavily restrictive with majority foreign equity permitted only in a handful export-oriented, high technology industries. Initiated reforms changed the perceptions of foreign investors with foreign investment policy becoming progressively liberal following steady withdrawal of external capital controls and simplification of procedures.

While India has an overall market-friendly and liberal policy towards foreign investment, foreign capital still does not enjoy equally easy access in all parts of the economy. The manufacturing sector is still untapped accompanied by lack of access in certain services and agriculture. India's future foreign investment policy faces the critical challenge of increasing access of foreign capital to these segments. Keeping in mind the issues relating to foreign investment, the study aims to achieve the following objectives:

- o To study the existing policy framework of International Investments.
- o To examine the economic policy determinants of FDI.