

## Robust Inward FDI into India in 2020-21 Augurs Well for Future Growth

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### The Context

The World Investment Report (WIR) 2020 by UNCTAD (United Nations Conference on Trade and Development) has projected a discouraging outlook for global FDI (Foreign Direct Investment) flows<sup>1</sup>.

An investment into a foreign firm is considered an FDI if it establishes a lasting interest. A lasting interest is established when an investor obtains at least 10% of the voting power in a firm. The key to foreign direct investment is the element of control. Foreign portfolio investment (FPI), refers to investments made in securities and other financial assets issued in another country.

UNCTAD defines FDI inflows as capital (equity) provided by foreign direct investor to a foreign affiliate, or capital received by a foreign direct investor from a foreign affiliate. Its definition therefore excludes reinvested earnings by foreign companies in their host country operations. The total inward FDI flows should comprise equity inflows, reinvested earnings, and other capital.

The WIR 2020 estimates that global inward FDI flows (according to the UNCTAD's definition) in 2019 of USD 1540 billion are likely to exhibit a drastic decline of between 30 and 40 percent in 2020, the Covid-19 Pandemic dominated year, to between USD 920 billion and USD1080 billion. Moreover, FDI inflows are projected to decline by further 5 to 10 percent in 2021. A rebound to positive growth is possible in 2022, but with a downward bias.

It is remarkable that in spite of the global subdued environment for the inward FDI, India has continued to exhibit robust inflows of FDI. In recent years, India has globally ranked in top 10 countries in FDI inflows. According to the Department for Promotion Industry and internal Trade (DPIIT), Government of India, India's total stock of FDI, comprising all three elements of FDI, noted above was USD 749.4 billion in December 2020. Equity flows accounted for around 72 percent, reinvested earnings around 22 percent, and other capital around 6 percent of the total capital stock. Healthy growth in total stock of FDI is indicated by about 50 percent of the stock accumulating between 2015-16 and 2020-21<sup>2</sup>.

With continuing strong inflows of FDI, India is expected to reach a milestone of inward FDI stock of USD 1000 billion in the next three to four years. This would then rank India comfortably in the top 15 countries in inward FDI stock globally.

According to the DPIIT source cited above, as of December 2020, the stock of portfolio investment by the Foreign Institutional Investors (FIIs) in equity and debt segments was USD 245 billion, about a quarter of which was accumulated between 2015-16 and 2020-21.

According to the Bombay Stock Exchange website, India's stock market capitalization on 25 May 2021 was INR 219.1 trillion (equivalent to USD 2.96 trillion at USD 1=INR 74), and the number of registered investors was 69 million<sup>3</sup>.

The WIR 2020 reports that India's outward flow of FDI was USD 12.1 billion in 2019, while the corresponding stock was USD 178.7 billion. With India rapidly integrating with the global economy, and the Indian companies increasingly seeking a global role for their supply chains, the flow and stock of outward flow is also expected to accelerate. The DPIIT is strongly urged to track India's outward FDI flows with the same granularity that it is tracking the inward FDI flows. India's trends in international trade also appear promising<sup>4</sup>.

Thus, in April 2021, first month of the financial year 2021-22, India's merchandise exports and imports were USD 30.6 billion, and USD 45.6 billion respectively, with a deficit of USD 15.1 billion. The corresponding figures for trade in service transactions were USD 21.2 billion and USD 13.0 billion respectively, with a surplus of USD 8.1 billion. Thus, for the two combines, India's total exports and imports were USD 51.8 and USD 58.7 billion, with a deficit of only USD 6.9 billion. If these averages are sustained for the whole of 2021-22 India's total international trade would be over USD 1326 billion as compared to USD 1010 billion in 2019.

### **Assessing India's Inward FDI Flows in 2020-21**

India's Ministry of Commerce released a statement on 24 May 2021 on India's FDI trends in 2020-21. It is this statement, reproduced on Public Information Bureau<sup>5</sup> which forms the basis of the discussion in this sub-section. Unless otherwise noted, the figures in this section, are from the above source. The Statement however is relatively brief and lacks disaggregated data which will take longer to compile. When compiled, the more granular data will be available on<sup>6</sup>.

The Ministry reported that India attracted the highest-ever total FDI inflow, comprising all three elements, equity flows, reinvestment, and other capital inflows, of USD 81.7 billion during 2020-21, an increase of 9.8 percent as compared to 2019-20, when total inflows were USD 74.4 billion. In FY 2020-21, the FDI equity inflow grew by 19 percent to USD 59.6 billion (73 percent of the total) compared to the previous year, when inflows were USD 50.0 billion (67 percent of the total). In view of the discouraging overall global FDI trends noted above, this is indeed a remarkable vote of confidence by the global community in India's economic management and its future growth prospects.

**FDI Originating Countries:** The Statement notes that, Singapore remained the largest source of FDI for the third consecutive year, with a share of 29 per cent. It was followed by the US with 23 per cent share, and Mauritius with 9 per cent. These three countries accounted for over three-fifths of total inward FDI in 2020-21.

Both Singapore and Mauritius are locations which are attractive for variety of investors from around the world, including some round-trilling of FDI by Indian citizens themselves. Therefore 'true' origin of FDI from the two countries does not get captured in official records.

The data available on inward FDI from April 2000 to December 2020 suggest that India received inward FDI from 72 countries. But with the exception of the above three countries, plus Netherlands, Japan, United Kingdom, Germany, UAE (United Arab Emirates), did the FDI inflow exceed even one percent of the total<sup>7</sup>.

The above analysis strongly suggests that more result-oriented initiatives are needed to diversify originator countries of India's FDI.

Out of top 10 countries, Saudi Arabia was the top investor in terms of percentage increase during 2020-21. It invested USD 2.8 billion in comparison to only USD 89.9 million in 2019-20. There was a promising rise of 227 per cent and 44 per cent recorded in FDI equity inflow from the USA and the UK, respectively.

**Sectors Attracting FDI:** 'Computer Software & Hardware' was the top sector during 2020-21 with around 44 percent share of the total FDI Equity inflow. This was followed by Construction (Infrastructure) Activities (13 percent), and Services Sector (8 percent) respectively. The major sectors, namely, Construction (Infrastructure) Activities, Computer Software & Hardware, Rubber Goods, Retail Trading, Drugs and Pharmaceuticals and Electrical Equipment have recorded more than 100 percent increase in equity inflows during 2020-21 as compared to the previous year.

The above sectoral composition of the inward FDI in 2020-21 is broadly consistent with priorities set under the Atmanirbhar Bharat Abhiyan, and Be-Vocal-for-local and for global strategic concepts<sup>8</sup>. Greater inflow of FDI in textile sector, in agriculture and food processing, and in medical equipment sector could further enhance congruence of these flows with India's current policy priorities. Additional FDI policy reforms, investment facilitation and measures to ease of doing business in these sub-sectors merits consideration.

**FDI Inflow Among the States:** The FDI inflows in 2020-21, as in earlier years, were highly concentrated. Gujarat was the top recipient of FDI among states, with 37 per cent share of total FDI equity inflows. It was followed by Maharashtra and Karnataka with 27 per cent and 13 per cent, respectively. Thus, these three states alone accounted for more than three fourths of total equity FDI in 2020-21.

Gujarat attracted the lion's share of inbound FDI under the computer software and hardware sector at 78 per cent. This was followed by Karnataka and Delhi at 9 per cent and 5 per cent, respectively. Gujarat is thus emerging as a newer location for computer software and hardware. This augurs well for Gujarat as this

pattern will also bring newer talent and ideas to Gujarat. Majority of the equity inflow of Gujarat has been reported in the sectors 'Computer Software & Hardware' (94 per cent) and Construction (Infrastructure) Activities (2 per cent) during 2020-21.

For the October 2019 to December 2020 period, only four states, Gujarat (31.9 percent), Maharashtra (27.6 percent), Karnataka (14.1 percent), and Delhi (10.8 percent) accounted for 84.4 percent of total inward FDI into India. More than 20 states, including Uttar Pradesh, West Bengal, Rajasthan, Punjab, Madhya Pradesh, Kerala, and Orissa attracted less than one percent of total inward FDI<sup>9</sup>.

While the above recorded FDI do not fully reflect in which state the FDI projects are actually undertaken as corporate headquarters are concentrated in Mumbai, Bangalore, and Delhi, a strong implication of the above geographical pattern of FDI is a strong need to diversify FDI inflows among the states. The states such as Uttar Pradesh, whose GSDP (Gross State Domestic Product) at INR 19.5 trillion (USD 268 billion), was the second highest in the country in 2020-21, in pursuing their ambitious developments will need to devise an effective and measurable strategy to enhance their share in India's inward FDI. This also applies to other states with high revealed priority to generate broad-based high economic growth.

### Concluding remarks

India's remarkable performance in attracting robust inflow of FDI in the Covid-19 dominated 2020-21, the period when Global FDI trends have been discouraging, deserves wider recognition. India however needs to diversify inward FDI inflow originating countries, broaden the sectors to which the FDI is flowing, and bringing them more in line with current policy priorities, especially in attracting inflows in textiles, medical equipment, agriculture, and tourism sectors. The Indian states, particularly those aspiring to climb the economic rankings rapidly such as Uttar Pradesh, and Madhya Pradesh, need to specifically devise strategies to obtain higher share of India's inward FDI.

It is strongly urged that the DPIIT initiate acquisition of capabilities to track India's outward FDI in a manner similar to its tracking of inward FDIs. India's goal of achieving USD 5 trillion economy would require Indian companies to be competitive globally in setting up supply chains, and in taking advantage of opportunities to enhance India's economic and strategic space globally. This requires cooperation among both the government agencies and businesses.

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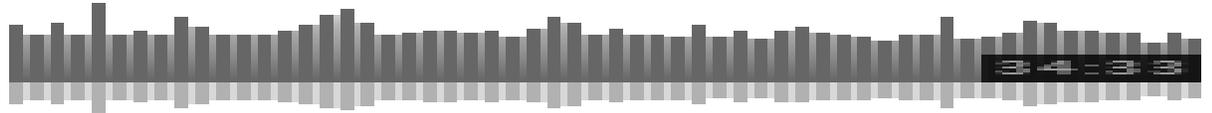
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