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THE POSITIVE INFLUENCE OF FDI INFLOW ON ECONOMIC GROWTH: AN EXPLORATORY COMPARATIVE INVESTIGATION OF INDIA & CHINA

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ABSTRACT

This paper is an attempt to investigate the economic growth in light of the effects of FDI inflow with special emphasis on two major developing countries of Asia, India and China during 2000-2017. There are many internal and external factors which influence the growth of an economy and one of them is FDI. Foreign Direct Investment facilitates capital investment to a lot of firms, and simultaneously further facilitates the generation of new technologies. It also generates employment opportunities & helps in gaining a competitive advantage through investing the foreign capital in the Indian economy. FDI also provides financial support to the firms. A series of determinants exist which actually accounts for FDI inflow including the existence of a big market, demand, qualitative labor force, and tax incentives. Furthermore, the service sector, telecommunication, IT hardware and software and construction development are a few additional industrial segments that extend facilitation in attracting FDI inflows. This investigation begins with evaluating the major countries contributing towards the development of the FDI inflow in Indo-China territories investigates the trend, major contributors apart from key sectors of FDI inflow in both Countries. In this study, the descriptive analysis is used to evaluate the targeted purposes.

Keywords: FDI; Developing Asia; India; China; Sources of FDI; Growth perspective; Market size; Low-cost labor force; Service sector.

INTRODUCTION

As a part of the economic liberalization process set in place by the Industrial Policy of 1991, the government of India opened up the retail sector to FDI through a series of steps. As far as development in the economic scenario is concerned, FDI contributes a major role in developing the economy. FDI provides access to the market, resources & also reduces the cost of production. FDI offers a source of external capital, employment generation & increased amount of profits which would further lead to economic development. Foreign companies invest directly in Indian businesses which are growing rapidly extending facilitation for improving the overall economic conditions.

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India & China, the two largest developing nations are emerging global players in today's dynamic environment in terms of economic growth rates, rising market share in the world, attracting more FDI's. In India, economic reforms started in 1991*(Shand &Bhide, 2000)* whereas in China it started in 1978 *(Ralph W. Huenemann, 2017)* which gave China, a competitive edge over India.

Javaid Dar (2013) referred that, In India, the future areas of growth are R&D, biotechnology, high-value IT-enabled services, agro-based industry whereas China has IT business, services & continued manufacturing as future areas of growth. India lacks behind China in attracting FDI because of political structure, infrastructural gap, monetary & fiscal policies, availability of capital etc. The key truth behind China's dominance as a preferred destination for attracting FDI is rapid economic development even from the reform period, infrastructural availability, abundance of labor & its availability at a lower cost. The ways in which India can attract more FDI is by political restructuring, promote agro-based export industries, remove corruption, accelerate privatization, provide monetary & fiscal benefits, remove FDI hurdles etc.

There exists a few key industrial segments that contribute significantly towards a high rate of investment in India; such as, infrastructure, automotive, manufacturing, pharmaceuticals, service etc., although these segments in China are manufacturing, real estate, business services & renting, wholesale & retail trade etc.

In this investigative study, the authors have significantly contributed a unique effort of differentiating between two economies i.e. India & China in terms of their FDI inflows & simultaneous influence over the development of the economy from the year 2000-2017. The structure of the paper goes with the identification of responsible factors for FDI growth in India & China followed by sources of FDI inflows and finally, findings and conclusion has been drawn.

LITERATURE REVIEW

Teli (2014) analyzed the trends & patterns of FDI inflows in India, also simultaneously analyzing the impact of FDI on economic indicators in India & finally to make projections of FDI in India & give necessary suggestions. This study concluded that FDI inflows show a positive trend over the period of time& it suggested that in coming years India may face stiff competition from foreign companies. (Goyal, 2017) identified the significant sources of FDI inflows & determinants which affect the growth of the Indian economy. This study concluded that there is a mixed trend of FDI inflow in India & as far as a favorable destination is concerned, India can still achieve it through liberalizing some of the policies, developing infrastructure & skilling the workforce.

Hasanand Barua (2013) compared the economic growth model of two countries & also identified the factors affecting the trade. This study also compared & analyzed the financial & economic reforms of the two countries. This study proved that China is much ahead of India in terms of FDI inflows & India is required to improve a lot for achieving sound FDI inflows. China has a huge potential in the IT service and outsourcing business whereas India still has a lot to prove in the manufacturing sector. Both China and India are nicely poised to become economic superpowers within the next 20 years.

Keshava (2008) analyzed the influence of FDI overgrowth, exports, GDI, FOREX in India. This study also focused on studying the behavior of factors in India & China that affect FDI & also to determine the way the Indian economy might benefit itself from China in order to make appropriate developments in the economy.

This research finally concludes that India is still lacking behind China in becoming an attractive destination for FDI inflows & to improve this condition India should make reforms that are beneficial for the economy. "China's success would also rely on its ability to carry out various reforms, to open up domestic markets, to improve the performance of the state-owned enterprise, to better protect intellectual property rights and to speed up the competition as well".

Sharma and Kaur (2013), in their study, emphasized the importance of empirical investigations of FDI– trade relationships for selected countries. "The study inculcates that there is strong evidence of unidirectional causality running from FDI to imports and from FDI to exports. FDI influences imports and exports but not caused by imports and exports.

Bi-causal relationship between imports and exports has been found in both the countries which suggests that India and China should focus more on technology imports and its transfer as an essential condition for expanding exports of these countries". The government of these countries should use this perspective of imports as an effective measure in the formulation of their export promotion strategy.

Dar and Singh (2014) examined the factors that help to make India and China the best FDI destinations among the developing countries and also found out the reasons for China performing better than India in terms of FDI attraction. GDP, FOREX, Exchange rate, inflation, etc. are found to be the main determinants of inflows of FDI across Indo-Chinese territories.

The authors in the present study also critically evaluated how FDI remained as a key determinant in influencing the level of economic growth in India.

Agrawal and khan (2011), in their study, attempted to evaluate the influence of FDI on the development of the Chinese and Indian economy. The relationship between FDI and economic growth has also been evaluated.

This study concludes that the factors included in this growth model were GDP, Human Resources, Workforce, Gross Capital Formation and FDI; GDP from whom was the dependent construct whereas the other four constructs were the independent constructs. This study further explored the key factors lying behind the huge display of FDI accumulation of China and also the key strategies that India may focus upon from the Chinese FDI growth story to effectively utilize FDI.

Quazi and Tandon (2015) compared the domestic investment climate in China and India. Further, the policies implemented in both countries have been studied."The analysis reveals that China fares better against India in terms of infrastructure, financial market, monetary system, corruption, and trade indicators".

Pavithran and Mukthar (2011) explained the SWOT analysis of India. A comparative analysis of China and India was conducted with reference to the international scenario. India's role in the international economic scenario has been less remarked comparatively than the arousal and dominance of China but increasingly India will be appreciated for the opportunities it is creating now-a-days". It was found that China is more successful than India in attracting FDI. But in recent years India is also gaining its place by a change in the perspective of investors.

Pillai and Rao (2013), in their study, identified the transnational attributes that constitute the major factor of FDI inflow to India. It also analyzed various determinants of FDI inflow to India.

Research Gap

Earlier researches have been done on the effects of FDI inflows in India, trends & patterns of inflows of FDI were also simultaneously analyzed, comparative analysis of FDI inflows over economic development in India & China but this study finds whether the FDI has an impact on GDP or whether GDP affects FDI.

Research Methodology

This study is descriptive in nature and the secondary data has been collected from the United Nations Conference on Trade and Development (UNCTAD) and the World Bank Report for the period ranging from 2000 to 2017. The collected data was presented in meaningful forms.

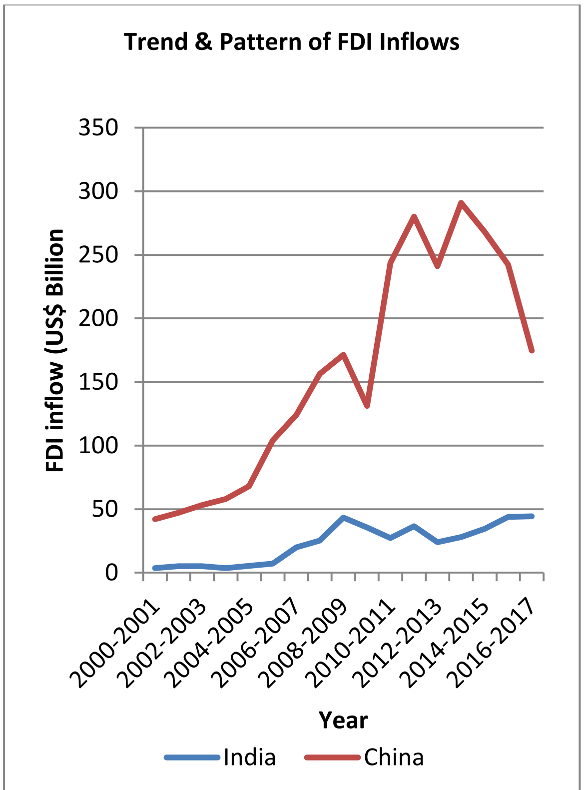
Inflows of FDI across India and China: Trend & Pattern

It is evident from the following Table 1 & Figure 1 that the growth of China has started a way far before even when the Indian economy not even liberalized. China has performed very well as a reason for which the economy has grown so well but they also saw continuous downfall from the year 2013-14 to 2016-17. Still, the development that India is doing in FDI inflow, and also the economic growth of India after its liberalization, is also commendable. Data of FDI inflows from April 2000 to March 2017 has been taken from The World Bank.

Table 1: India & China FDI inflow from April 2000- March 2017

Session	India(in US$ Billion)	China(in US$ Billion)
2000-2001	3.584	42.095
2001-2002	5.128	47.053
2002-2003	5.209	53.074
2003-2004	3.682	57.901
2004-2005	5.429	68.117
2005-2006	7.269	104.109
2006-2007	20.029	124.082
2007-2008	25.228	156.249
2008-2009	43.406	171.535
2009-2010	35.581	131.057
2010-2011	27.397	243.703
2011-2012	36.499	280.072
2012-2013	23.996	241.214
2013-2014	28.153	290.928
2014-2015	34.577	268.097
2015-2016	44.009	242.489
2016-2017	44.459	174.750

Source: World Development Indicator, The World Bank Report



Source: Official national sources & United Nations Conference on Trade & Development (UNCTD).

Figure 1: Trend & Pattern of FDI inflows in India & China

From figure-1 we can see the difference in the inflows of FDI in India & China. There is a huge gap existing which needs to be covered by India and is actually an intensely tough task but India is trying its level best to achieve what it can.

Comparing GDP of India & China

"India is developing into an open-market economy, yet traces of its past policies remain whereas China has moved from a closed, centrally planned system to a more market-oriented one that plays a major global role. China continues to pursue an industrial policy, state support of key sectors, and a restrictive investment regime. Still, China's per capita income is below the world average.

Rising macroeconomic imbalances in India and improving economic conditions in Western countries led investors to shift capital away from India, prompting a sharp depreciation of the rupee through 2016". (Index Mundi- CIA factbook)

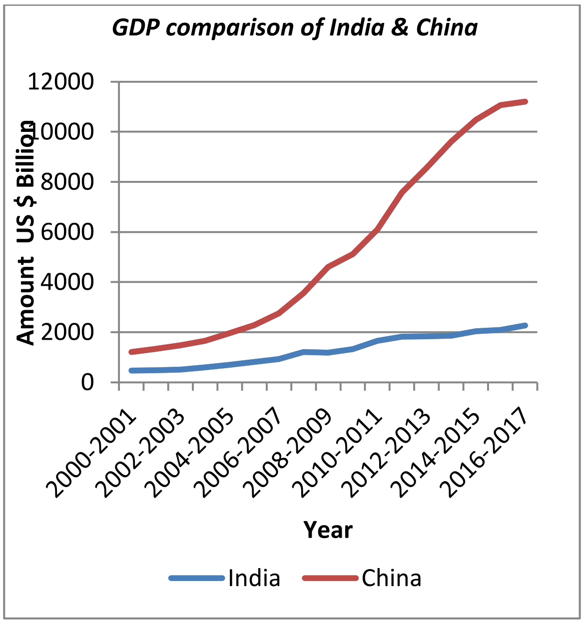
Table 2 – GDP (US$ Billion)

YEAR	India	China
2000-2001	462.15	1211.35
2001-2002	478.97	1339.4
2002-2003	508.07	1470.55
2003-2004	599.59	1660.29
2004-2005	699.69	1955.35
2005-2006	808.9	2285.97
2006-2007	920.32	2752.13
2007-2008	1201.11	3552.18
2008-2009	1186.95	4598.21
2009-2010	1323.94	5109.95
2010-2011	1656.62	6100.62
2011-2012	1823.05	7572.55
2012-2013	1827.64	8560.55
2013-2014	1856.72	9607.22
2014-2015	2035.39	10482.37
2015-2016	2089.87	11064.67
2016-2017	2263.79	11199.15

Source: tradingeconomics.com | World Bank updated on 28 June 2018

From table 2 it is evident from the above data that India's growth begins at a lower level of utilizing the resources. Therefore, it can raise GDP growth by providing better employment opportunities with existing technologies. China's economy begins at a very high resource utilization level. Therefore, it can no longer raise GDP growth by only utilizing the existing technologies."

It must innovate repeatedly, which is not easy when compared with China's current economic structure where most of its economic sectors are under direct or indirect government control". In the last four years, India gained 20 points in the global competitiveness rankings, while China's ranking remained roughly unchanged. (World Economic Forum)



Source -tradingeconomics.com | World Bank updated on 28 June 2018

Figure 2: GDP comparison of India and China

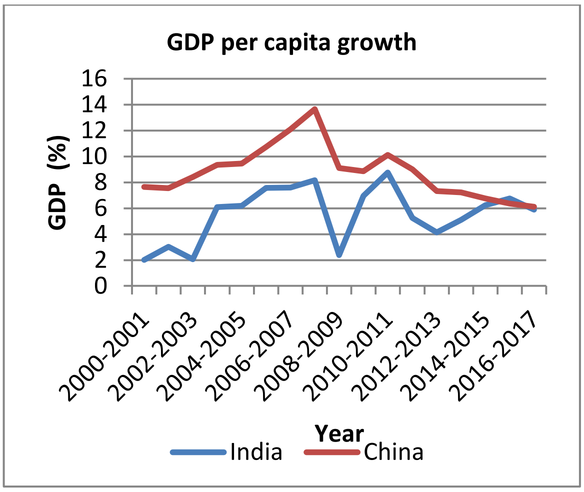
From figure-2 we can see that China is developing at a very high pace whereas India is still lagging far in comparison to that of China but the growth that India reflected during 2000 to 2017 is tremendous. India is on the verge of a digital revolution. The Indian economy still has less government control over it than the Chinese economy that is why India has more scope for development than China.

Table 3: GDP per capita growth (annual %)

YEAR	India	China
2000-2001	2.016	7.64
2001-2002	3.021	7.556
2002-2003	2.058	8.402
2003-2004	6.087	9.352
2004-2005	6.188	9.459
2005-2006	7.567	10.743
2006-2007	7.585	12.092
2007-2008	8.154	13.636
2008-2009	2.375	9.094
2009-2010	6.95	8.857
2010-2011	8.763	10.103
2011-2012	5.249	9.013
2012-2013	4.135	7.332
2013-2014	5.097	7.227
2014-2015	6.234	6.756
2015-2016	6.756	6.358
2016-2017	5.884	6.113

Source: World Bank national accounts data, and OECD National Accounts data files.

From table 3 GDP per capita growth annual percentage has been evaluated from World Bank National accounts data, & it can be seen that India has overall attained approximately 3% growth from 2000-2017 whereas China's overall GDP percentage has been devaluated. From this perspective, it is seen that India is growing more rapidly in their economy whereas the economy of China is not growing.



Source: World Bank national accounts data, and OECD National Accounts data files.

Figure 3: GDP per capita growth (annual %)

From the above figure, it can be drawn that India who started very late in comparison to China in terms of GDP has rapidly moved ahead from China in economic growth. India has much more soft power than China. In fact, Chinese soft power is limited to food & NYT. And finally, the Chinese economy is a tough competition for India & both are challenging each other equally to be ahead of the other one.

Next thing is to identify the sectors on which the developmental inflow of FDI majorly depends.

The following table shows different sectors of China & the number of enterprises that are indulged in that particular section which contribute towards the FDI inflow.

Table – 4: Major sectors that generate FDI inflows in China

Sector	No. of enterprises
Wholesale & retail	12,283
Leasing & business services	5,087
Manufacturing	4,986
Information transmission, computer services, software	3,169
Real estate	737
Agriculture, forestry, animal husbandry, fishing	706
Transport, storage, post & telecommunication services	517
Production & supply of electricity, gas & water	372
Services to household & other services	349

Source: Statista- The Statistics Portal, 2017

The above table shows that China possesses a huge volume of enterprises in the Wholesale & retail sector & China' is one of the most attractive destinations for investment. In China capital rests on its development of infrastructure, resource availability, productivity and workforce skills, and the development of the business value chain as it is clearly seen from the above table that manufacturing firms have higher no of enterprises which means it is a major sector of China for the inflow of FDI.

Table – 5: The inflow of FDI in India across various sectors

Sector	%age of Total Inflows
Service	17.46
Telecommunications	8.4
Computer Software & Hardware	7.76
Construction Development: Townships, housing, built-up infrastructure and construction-development projects	6.9
Automobile Industry	5.01
Trading	4.38
Drugs & Pharmaceuticals	4.36
Chemicals (Other Than Fertilizers)	3.97
Power	3.44
Construction (Infrastructure) Activities	2.99

Source: Quarterly Fact Sheet on FDI (From April 2000 to September 2017), Department of Industrial Policy and Promotion Ministry of Commerce and Industry Government of India

India is the fifth-largest economy across the globe and ranks third in GDP in entire Asia, which is one of the factors responsible for FDI Inflows in India. India is a country which provides a lot of opportunities for foreign companies to become the global player in terms of employment generation availability of material as the portion that is contributed towards service sector is very huge in comparison to all other sectors.

Now we will see which are the most investing countries in both India & China:

Table 6: Major investing countries in China & India

Main Investing Countries in CHINA	%**age**
Hong Kong	69
Singapore	5
South Korea	4
USA	3
Macao	3
Taiwan	3
Japan	3
Germany	2
UK	2
Luxembourg	1

Source: Invest in China, 2018Source: Quarterly Fact Sheet on FDI (FromApril, 2000 to September, 2017), Department of Industrial Policy and Promotion Ministry of Commerce and Industry Government of India

Main Investing Countries in INDIA	%**age**
Mauritius	34.45
Singapore	16.76
Japan	7.45
United Kingdom	6.97
Netherlands	6.33
U.S.A	6.06
Germany	2.98
Cyprus	2.62
France	1.69
UAE	1.39

The percentage of 69 made Hong Kong the most investing country in China. This means more than half of the FDI inflow to China is from Hong Kong whereas India only gets 34.45% as the highest portion of the FDI inflow from Mauritius. Then the existence of some more countries are observed that also provide investment in both countries. China also gets investment from Singapore, South Korea, USA, Macao, Taiwan etc. These are the top investors in China. Singapore, Japan, UK, Netherlands, USA are few countries which have an investment in India through FDI.

Government Initiatives:
A recent report released by the Ministry of Commerce of China said that FDI in China increased by 9.8 percent between January to November 2017. It has also been announced that China will permit fully owned foreign-invested enterprises in special vehicle apart from unique energy vehicle manufacturing industry to be set up since June 2018 in Pilot Free Trade Zones in China. After a series of measures to promote FDI inflow, China is expecting more foreign investment

The Government of India made several updations across its FDI policy framework in order to boost its FDI inflow. The government raised the upper limit of foreign investment from 26 percent to 49 percent in insurance sector in the year 2014. The government also initiated "Make in India" initiative in the same year. As of April 2015, the inflow of FDI in India increased by 48% after the start of the governments' "Make in India" initiative. The Government of India is likely to allow 100% FDI in cash and ATM management companies since they are not required to comply with the Private Securities Agencies Regulations Act (PSARA).

CONCLUSION:
FDI helps companies to progress into new markets as a result of globalization. Both India & China are facing a tough competition. Over past 17 years that is from 2000-2017 it has been observed that the performance of India has increased significantly over these years & there is still much more to come. Growth in China is constant but India's growth is not that much significant, it fluctuates due to a small factor to a great extent. And we already know that China is much way ahead of India in almost every way, say, in terms of growth, in terms of infrastructure etc. But when we talk about GDP as an annual percentage we see that India is giving a very tough competitive challenge to China and even India is ahead during 2017 from China in GDP annual growth.

China is required to gain FDI in the services sector because China possesses much lesser number of enterprises in their economy, whereas India needs to focus on the Construction sector & to improve it Govt. has taken some initiatives as well like implementing the policies. At last, this study concludes that there is relatively high competition between these two economies & both are trying hard to be the best from each other.

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