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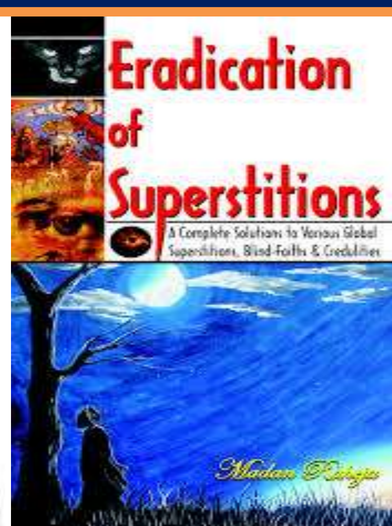

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FOREIGN DIRECT INVESTMENT IN INDIA: TRENDS, DETERMINANTS AND CHALLENGES

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ABSTRACT:

The present study attempts to empirically examine the challenges and issues of FDI in India by taking time series data for the period 1992-93 to 2008-09. It applies Ordinary Least Square (OLS) method for this purpose. India has adopted liberalization policy during 1999. After liberalization India emerged as leading nation and attracted maximum FDI. In this paper an attempt is made to analysis the impact of 51% FDI in multi brand retail in Indian economy.

Keywords*: Foreign Direct Investment, Inflation, Gross Domestic Product, Spillover, Trade Openness, Foreign Exchange Reserves*

INTRODUCTION

Recently a significant step has been taken towards liberalizing India's retail sector by 51% FDI in single brand retailing. A move that should pave way for big name like Nike, Versace, Addidas, Marks & Spencer to set up their own stores in India. This means that foreign companies willing to enter in the Indian market will now be able to invest up to 51% in setting up production facility, distribution network and retail shop and rest will come for Indian investor. Optimistic on the other hand see a whole range of opportunities from improved collection processing and better distribution of farm products to generation of more opportunitiesfor the rural and urban unemployed. The recent global financial economic crisis has had dampening effect on FDI. The inflow and outflow of FDI has become an upcoming ideology in the international economics which has changed all parameter of the economic theory. It has become penculin of all economic problems.

Foreign Direct Investment (FDI) also plays an important role in accelerating the pace of economic growth. FDI provides the much needed foreign exchange to help the bridge the balance of payment or trade deficit. FDI brings complementary assets such as technology, management and organizational competencies and there are spillover effects of these assets on the rest of the economy. FDI is treated as a main engine of economic growth and technological development which provides ample opportunities in accelerating economic development. FDI contributes to exports directly and an enhanced export possibility contributes to the growth of the host economies by relaxing demand side constraints on economic growth. FDI according to UNCTAD implies that the investor exerts a significant degree of influence on the management of enterprise resident in the other economy. Encouragement of FDI is an integral part of the economic reforms process of developing nations because it is seen as an instrument of technology transfer, managerial skill, and augmentation of foreign exchange reserves and globalization of the economy. Economic growth, continuing trade regimes and increased competition among firms are likely to derive the global expansion of MNC activity.

The present paper has been divided into five sections. Section- I is devoted to survey of literature. Section-II analyzes the trends and pattern of FDI in India. Section-III discusses the main determinants of FDI in Indian economy for the period 1992-93 to 2008-09. Section –IV discusses the main challenges of FDI in Indian economy. The main conclusions emerging out of the study are presented in Section- V.

SECTION - I

SURVEY OF LITERATURE

Many empirical studies have been undertaken to analyze the trends and determinants of Foreign Direct Investment (FDI) in India, few of them are as follows:-

Ana Mar (1997)[1] reviews the recent evidence on the scale of FDI to low-income countries over the period 1970-96 and major factors determining foreign companies' decision to invest in a particular country. The study concludes that large market size, low labor costs and high return in natural resources are amongst the major determinants in decision to invest in low income countries.

Mucchielli and Soubaya (2000)[2] investigated the determinants of the volume of trade of the French Multinational Corporations (MNCs). The major findings suggest that inward FDI has a positive influence on Foreign trade (including exports and imports), and this positive influence is stronger for exports compared with imports.

Charkraborty and Basu (2002)[3] explore the co-integration relationship between net inflows of FDI, real GDP, unit cost of labor and the proportion of import duties in tax revenue for India with the method developed by Johansen (1990). They find two long-run equilibrium relationships. The first relationship is between net inflow of FDI, real GDP and the proportion of import duties in tax revenue and the second is between real GDP and unit cost of labor. They find unidirectional Granger Causality from real GDP to net inflow of FDI.

Naga Raj (2003)[4] discusses the trends in FDI in India in the 1990s and compare them with china. The study raises some issues on the effects of the recent investments on the domestic economy. Based on the analytical discussion and comparative experience, the study concludes by suggesting a realistic foreign investment policy.

Salisu A.A. fees (2004)[5] examined the determinants and impact of FDI on economic growth in developing countries using Nigeria as a case study. The study observed that inflation, debt burden, and exchange rate significantly influence FDI inflows into Nigeria. The contribution of FDI to economic growth in Nigeria was very low even though it was perceived to be a significant factor influencing the level of economic growth in Nigeria

Kulwinder Singh (2005)[6] analyzed the developments (economic and political) in India relating to the trends in two sectors:- Industry and Infrastructure. The study concludes that the impact of the reforms in India on the policy environment for FDI presents a mixed picture. The industrial reforms have gone far, though they need to be supplemented by more infrastructure reforms, which are a critical missing link.

Nirupam Bajpai and Jeffrey D. Sachs (2006)[7] attempted to identify the issues and problems associated with India's current FDI regimes, and more importantly the other associated factors responsible for India's unattractiveness as an investment location. Despite India offering a large domestic market, rule of law, low labor costs, and a well working democracy, her performance in attracting FDI flows have been far from satisfactory. The conclusion of the study is that a restricted FDI regime, high import tariffs, exit barriers for firms, stringent labor laws, poor quality infrastructure, centralized decision making processes, and a very limited scale of export processing zones make India an unattractive investment location.

Nandita Dasgupta (2007)[8] examined the effects of international trade and investment related macro-economic variables, namely, exports, imports and FDI inflows and the outflows of FDI from India over 1970 through 2005. Unidirectional Granger Causality was found from export and import to FDI outflows, but no such causality exists from FDI inflows to the corresponding outflows from India.

Burak Camurdan and Ismail Cevis (2009) [9]developed an empirical framework to estimate the economic determinants of FDI inflows by employing a panel data set of 17 developing countries and transition economies for the period of 1989-2006. Seven independent variables were taken for this research namely, the previous period FDI, GDP growth rate, wage, trade rate, inflation rate and economic investment. The empirical results conclude that the previous period FDI is important as an economic determinant. Besides, it is also understood that the main determinants of FDI inflows are Inflation rate, the interest rate and trade (openness) rate.

Sapna Hooda (2011)[10] analyzed the impact of FDI on economic growth of Indian economy for the period 1991-92 to 2008-09. She used OLS method for this purpose. The empirical results found that foreign Direct Investment (FDI) is a vital and significant factor influencing the level of growth in Indian economy. She also estimated the determinants of FDI inflows and found that trade GDP, Research and Development GDP, Financial position, exchange rate, Reserves GDP are the important macroeconomic determinants of FDI Inflows in India.

SECTION-II TRENDS AND PATTERN OF FDI IN INDIA (1991-2008)

At the time of its independence in 1947, India was a host to a significant stock of Foreign Direct Investment (FDI) largely owed to her est. while colonial master: the UK. Soon after the independence, India embarked on a strategy of industrialization with active governmental intervention. Domestic enterprise accumulated considerable capability in the process of industrialization, which has influenced not only the pattern of inward FDI in the country in subsequent period but has also led to investments made by Indian enterprises abroad. The changes in government policy have also had an important bearing on the FDI position of India. Foreign Investment plays on important role in the long-term economic development of a country by:-

1. Augmenting availability of capital
2. Enhancing competitiveness of the domestic economy through transfer of technology
3. Strengthening infrastructure and Boosting exports
4. Raising Productivity and Generating new employment opportunities

Foreign investment therefore, is a strategic instrument of development policy. The initial policy stimulus to Foreign Direct Investment (FDI) in India came in July 1991 when the new industrial policy provided, inter alia, automatic approval for projects with foreign equity participation up to 51 percent in high priority areas. In the wake of economic liberalization policy initiated in 1991, the government of India has taken several measures to encourage foreign investment both Direct and Portfolio, in almost all sectors of the economy. However, the emphasis has been on Foreign Direct Investment (FDI) inflows in the:-

1. Development of infrastructure
2. Technological up gradation of Indian Industry
3. Projects having the potential for creating employment opportunities on a large scale and,
4. Setting up Special Economic Zones (SEZs) and establishing manufacturing units therein.

India has consistently been classified as one of the most attractive investment destinations by reputed international rating organizations. With a vast reservoir of skilled and cost-effective manpower, India offers immense opportunities for Business Process Outsourcing (BPO), Knowledge Process outsourcing (KPO) and Engineering Process Outsourcing (EPO). In recent years, the Government has initiated the second generation reforms under which measures have been taken to further facilitate and broaden the base of FDI in India. The policy for FDI allows freedom of location, choice of technology, repatriation of capital and dividends. As a result of these measures, there has been a strong surge of international interest in the Indian economy. The rate at which FDI inflow has grown during the post-liberalization period is a clear indication that India is fast emerging as an attractive destination for overseas investors.

INDIA'S SHARE IN WORLD FOREIGN DIRECT INVESTMENT (FDI):-

Trend in value of India's Foreign direct Investment against the background of trends in world's FDI are presented in following Table **(1.1):-**

TABLE:-1.1 INDIA'S PERCENTAGE SHARE IN WORLD FDI

Year	WORLD FDI (MILLIONS OF DOLLARS)	INDIA'S FDI (MILLIONS OF DOLLARS)	% SHARE OF INDIA IN WORLD FDI
1991	158428	155	0.09
1992	170398	261	0.15
1993	219421	550	0.25
1994	253506	973	0.38
1995	328862	2144	0.65
1996	358869	2426	0.67
1997	464341	3351	0.72
1998	643879	2258	0.35
1999	1075049	2154	0.20
2000	1270764	2315	0.18
2001	817574	3403	0.41
2002	678751	3449	0.50
2003	559576	4269	0.76
2004	742143	5771	0.77
2005	945795	6676	0.70
2006	1305852	16881	1.29
2007	1978838	25127	1.26
2008	1697353	41554	2.44

SOURCE:-World Investment Report (Various Issues) Published by United Nations, New York and Geneva.

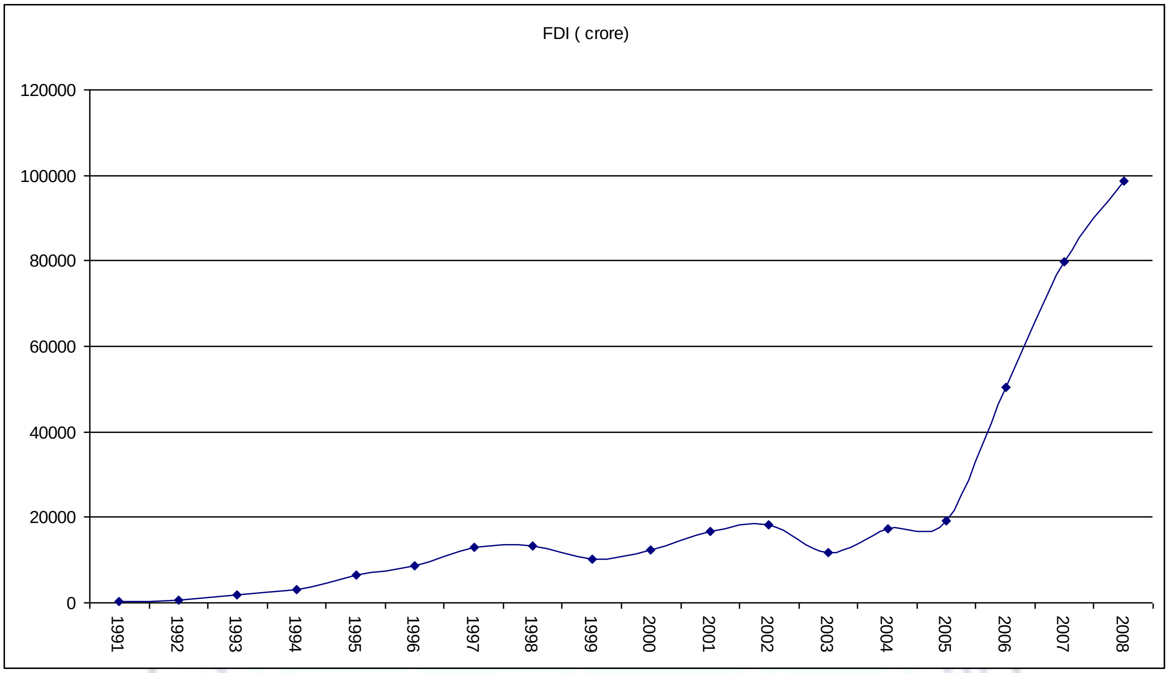
The above table (1.1) shows that India's share in world FDI has been rising continuously since 2001. The share was only 0.09 percent in 1991 and rose to 1.29 percent in 2006 and 2.44 percent in 2008. India's share in world FDI was very high in 2008 due to reform in policies, better infrastructure, and more vibrant financial sector.

TABLE:-1.2 TRENDS IN FDI INFLOWS IN INDIA (1991-2008):-

YEAR	FDI (₹ crore)	FDI GROWTH %
1991	353	-
1992	691	95.75%
1993	1862	169.46%
1994	3112	67.13%
1995	6485	108.38%
1996	8752	34.95%
1997	12990	48.42%
1998	13269	2.14%
1999	10167	-23.37%
2000	12354	21.51%
2001	16778	35.81%
2002	18195	8.44%
2003	11617	-36.15%
2004	17266	48.62%
2005	19299	11.77%
2006	50357	160.93%
2007	79735	58.33%
2008	98664	23.73%

SOURCE:- Own calculation

FIG:-1.1 TRENDS IN FDI INFLOWS IN INDIA (1991-2008):-



The above table (1.2) and fig (1.1) shows that Foreign Direct Investment inflows (FDI) have gone up significantly in Post-Reform era undoubtedly due to radical changes in the policies that have increased the confidence of the investors. The FDI inflow simply doubled in first year of reforms in 1992 to 691 ₹ crore as compared to ₹ 353 crore in 1991. As for FDI growth, it is not a smooth one. There are ups and down in the growth % of FDI during 1991 to 2008. In the two years 1999 and 2003 the growth rate is found to be negative. The reduction in FDI inflows in the Indian economy after 1997-98 is due to the effect of East Asian Crisis. However, the growth rate become positive from the year 2004 and during 2006, it was very high. It again decreases in 2007 and 2008 due to economic crisis.

ROUTES FOR INWARD FLOWS OF FOREIGN DIRECT INVESTMENT

Foreign Direct Investment (FDI) into India is allowed through two channels:-

1. **Automatic Route**
2. **Government Approval Route**

AUTOMATIC ROUTE:-

FDI under automatic route does not require prior approval either by the Govt. of India or the Reserve Bank of India (RBI). Investors are only required to notify the concerned Regional office of RBI within 30 days of receipt of Inward remittances and file required documents with that office within 30 days of issue of shares to foreign investors.

The automatic approval route of the RBI was introduced to facilitate FDI inflows. However, during post-policy period, the actual investment flows through the automatic route of the RBI against total FDI flows remained rather insignificant. This was partly due to the fact that crucial areas like electronics, services and minerals were left out of the automatic approval route. Another limitation was the ceiling of 51 per cent on foreign equity holding. An increasing number of proposals were cleared through the FIPB route while the automatic approval route was relatively unimportant. However, since 2000 automatic approval route has become significant and accounts for a large part of FDI inflows.

GOVERNMENT APPROVAL:-

Especially since For the following categories, Government approval for FDI through the Foreign Investment Promotion Board (FIPB) is necessary:-

- **i.)** Proposals attracting compulsory licensing
- **ii.)** Items of manufacturing reserved for the small scale sector
- **iii.)** Acquisition of existing shares.

FIPB ensures a single-window approval for the investment and acts as a screening agency. FIPB approvals are normally received in 30 days. RBI introduced automatic approval system in 1992 to facilitate more convenient entry to foreign investors. From 1996, a FDI inflow on acquisition of shares has also been included and has been rising continuously since 2004 whereas FDI Inflows through NRI's route have been declining 2002.

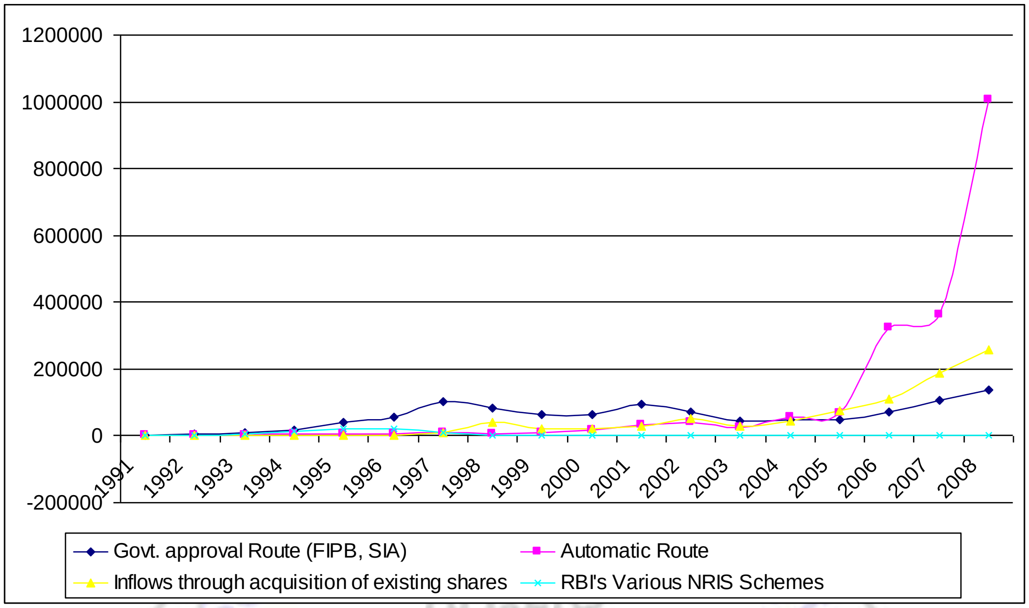
TABLE: 1.3 STATEMENT ON ROUTE WISE FDI INFLOWS (1991-2008) (US$ Million)

Year Jan.-Dec.)	I	II	III	IV	Total (I to IV)
	Govt. approval	Automatic Route	Inflows through	RBI's Various	

	Route (FIPB, SIA)		acquisition of existing shares	NRIS Schemes	
1991	1912	-	-	1623	3535
1992	4907	475	-	1530	6912
1993	10414	2411	-	5795	18620
1994	16044	3626	-	11452	31,122
1995	39674	5302	-	19878	64854
1996	57667	6196	3083	20621	87522
1997	101284	8677	9540	10397	129898
1998	82397	6107	40594	3594	132,692
1999	61895	7608	19608	3488	92599
2000	63368	16975	20581	3487	104,411
2001	96386	32411	29622	2292	160,711
2002	69580	39030	52623	111	161,344
2003	42956	23399	29284	-	95639
2004	48517	54221	45076	-	147814
2005	49728	68687	74292	-	192707
2006	69683	321758	112132	-	503573
2007	107873	361002	186075	-	654950
2008	135588	1004681	256986	-	1397255

SOURCE:- RBI, (FED) Central office, Mumbai

FIG:-1.2 ROUTE WISE FDI INFLOWS IN INDIA (1991-2008)



The above table (1.3) and fig (1.2) shows that the FIPB route-represents larger projects which require bulk of Inflows and account for Government's discretionary approval. Although, the share of FIPB route is declining somewhat as compared to RBI's automatic route and acquisition of existing shares. Automatic approval route via RBI shows an upward trend since 1995. This route is meant for smaller sized investment projects. Acquisitions of existing shares have also shown an increasing trend but FDI inflows through NRI's route have shown a sharp declining trend.

FDI APPROVALS AND ACTUAL INFLOWS:-

For almost a decade since 1991, FDI inflows as a proportion of FDI approvals have ranged between 20 percent and 50 percent. The impediments to implementation of FDI approvals reside both at the centre and with state Governments with their own obstructionist bureaucracies and corrupt political establishments. In an effort to bridge the gap between FDI approvals and actual inflows, the Government set up the Foreign Investment Implementation Authority (FIIA) in 1999, designed to function as a fast-track facilitation device to help foreign investors, clear bureaucratic hurdles at the central and state levels.

The below table (1.4) shows that FDI approvals as well as actual flows have been showing upward trend from 1991-92 to 1998-99. Actual inflow were merely 165 US$ million in 1991-92 and reached to 3083 US$ million in 1998-99. During the period 1998-99 to 2004-05, FDI approvals have been showing downward trend except for the year 2000-2001. The share of actual inflow as a per cent of approvals has been rising rapidly since 2001-02 but it again showed a downward trend during 2004-05.

TABLE:-1.4 FOREIGN DIRECT INVESTMENT APPROVALS AND INFLOWS

Year	APPROVALS (US$ Million)	INFLOWS (US$ Million)	ACTUAL INFLOW AS A % OF APPROVALS
1991-92	527	165	31.3
1992-93	1976	393	19.8
1993-94	2428	654	26.9
1994-95	3178	1374	43.2
1995-96	11439	2141	18.7
1996-97	11484	2770	24.1
1997-98	10984	3682	33.5
1998-99	7532	3083	40.9
1999-2000	4266	2439	57.2
2000-01	5754	2908	50.5
2001-02	3160	4222	133.6
2002-03	1654	3134	189.4
2003-04	1353	2776	205.1
2004-05	1475	2549	172.8

SOURCE:- Economic Survey (Various issues)

SOURCES OF FDI IN INDIA

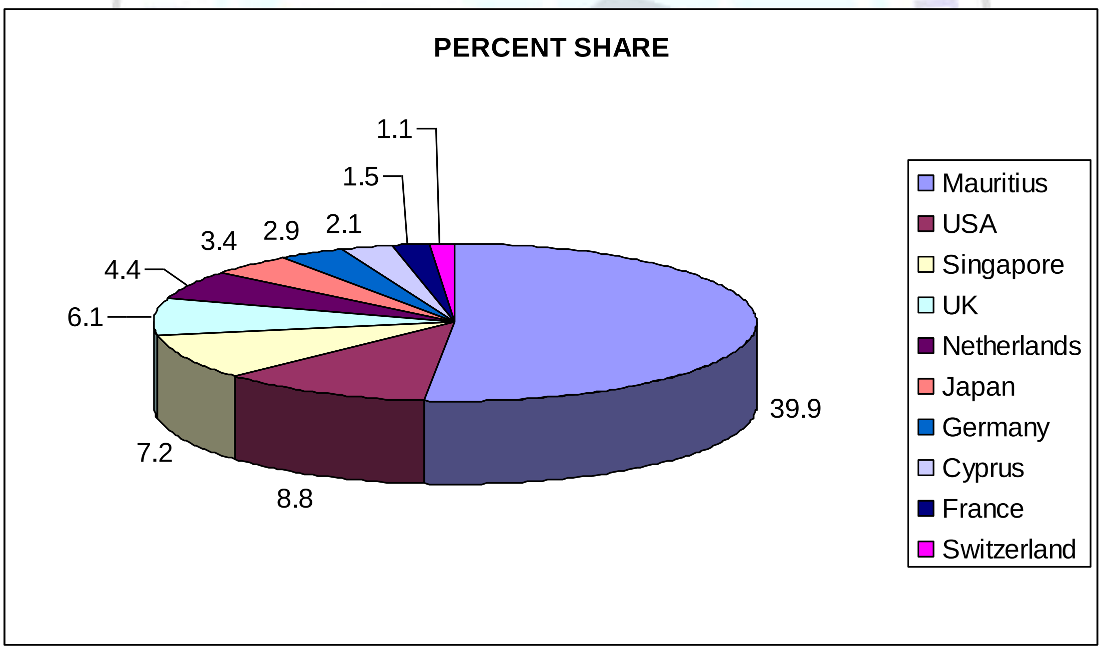
India has broadened the sources of FDI in the period of reforms. There were 120 countries investing in India in 2008 as compared to 15 countries in 1991. Thus the number of countries investing in India increased after reforms. After liberalization of economy Mauritius, South Korea, Malaysia, Cayman Islands and many more countries predominantly appears on the list of major investors apart from U.S., U.K., Germany, Japan, Italy, and France which are not only the major investor now but during pre-liberalization era also.

TABLE:- 1.5 MAJOR SOURCES OF FDI IN INDIA (1991-2008)

COUNTRY	PERCENT SHARE
Mauritius	39.9
USA	8.8
Singapore	7.2
UK	6.1
Netherlands	4.4
Japan	3.4
Germany	2.9
Cyprus	2.1
France	1.5
Switzerland	1.1

SOURCE: ECONOMIC SURVEY (VARIOUS ISSUES)

FIGURE: 1.3 MAJOR SOURCES OF FDI IN INDIA (1991-2008)



The above table (1.5) and fig (1.3) shows that Mauritius is the largest investor in India during 1991-2008. FDI inflows from Mauritius constitute about 39.9% of the total FDI in India and enjoying the top position on India's FDI map from 1995. This dominance of Mauritius is because of the Double Taxation Treaty i.e. DTAA- Double Taxation Avoidance Agreement between the two countries, which favors routing of investment through this country. This (DTAA) type of taxation treaty has been made out with Singapore also. The US is the second largest investing country in India. While comparing the investment made by both (Mauritius and US) countries one interesting fact comes up which shows that there is a huge difference (between FDI inflows to India from Mauritius and the US) in the volume of FDI received from Mauritius and the US. FDI inflow from Mauritius is more than double then that from the US. The other major countries are Singapore with a relative share of 7.2% followed by UK, Netherlands, Japan, Germany, Cyprus, France, and Switzerland.

SECTION-III

DETERMINANTS OF FOREIGN DIRECT INVESTMENT (FDI) IN INDIA (1992-93 to 2008-09)

In the present section, we have empirically examined the major factors which have determined the inflows of FDI in India in the Post-Reform period i.e. 1992-93 to 2008-09. A country which has a stable macroeconomic condition with high and sustained growth rates will receive more FDI inflows than a more volatile economy. The variable that measures the economic stability and growth are Gross Domestic Product (GDP), inflation rates, Trade Openness and Foreign exchange reserves. Investors prefer to invest in more stable economies that reflect a lesser degree of uncertainty and risk. Market size also plays an important role in attracting Foreign Direct Investment (FDI) from abroad and it is measured by GDP. Market size tend to influence the inflows, as an increased customer base signifies more opportunities of being successful and also the fact that with the rampant development the purchasing power of the people has also been greatly influenced moving to many levels higher in comparison to what it was before the economic growth.

Trade openness is also considered to be one of the key determinants of FDI as represented in the past literature; much of FDI is export oriented and may also require the import of complementary, intermediate and capital goods. Thus, trade openness is generally expected to be a positive and significant determinant of Foreign Direct Investment (FDI).

METHODOLOGY, DATA AND MODEL BUILDING:-

The period taken for the study is post-liberalization period i.e. from 1992-93 to 2008-09 because the economic liberalization was initiated under finance minister Manmohan Singh from 1991 onwards. FDI started flowing into the country with the significant proportions with the introduction of economic reforms. Multiple regression analysis has been used to find out the determinants of FDI in India for the period 1992-93 to 2008-09. In the regression model the dependent variable is FDI in India and the independent variables considered in the model are Gross Domestic Product (GDP), Trade Openness, Inflation and Foreign exchange reserves. We have used data on wholesale Price Index (WPI) for measuring inflation. All the relevant data is obtained from Handbook of Statistics on Indian Economy (various issues), Reserve Bank of India Bulletin (Various issues), Economic Survey (various issues), International Financial statistics yearbook (various issues) etc. we have applied Ordinary Least Square (OLS) method of estimation. The Double log transformations for each of these models are fitted and specified. The prime objective of generating double log transformation regression equations or natural log transformation (i.e. log to the base e, where e = 2.718 approx) is to determine the degree of sensitivity of the dependent variable to change in the explanatory variables.

MODEL BUILDING:-

The model can be written as:-

$$\textbf{FDI} = f\,(\textbf{GDP, TO, INF, FOREX}) \qquad \textbf{(1)}$$

Where,

FDI = Foreign Direct Investment

GDP = Gross Domestic Product

TO = Trade Openness

INF = Inflation (WPI)

FOREX = Foreign Exchange Reserves

More precisely, the variable to the left-hand side of the equality symbol represents the dependent variable, while those to the right-hand side are referred to technically as explanatory variable. The logarithmic transformation of estimated model is:-

$$\ln FDI = bo + b_1 \ln GDP + b_2 \ln TO + b_3 \ln INF. + b_4 \ln FOREX + + Ui \quad (2)$$

In the present study, instead of using linear regression equations we have used Natural logarithmic equations hence the study is concerned with isolating the effects of changes in explanatory variables on FDI inflows in Indian economy.

SECTION-IV

MAJOR ISSUES AND CHALLENGES OF FDI IN INDIA

In addition to India's poor performance in terms of competitiveness, quality of infrastructure, and skills and productivity of labor, there are several other factors that make India a far less attractive ground for direct investment than the potential she has. Given that India has a huge domestic market and a fast growing one, there is every reason to believe that with continued reforms that improve institutions and economic policies, and thereby create an environment conducive for private investment and economic growth that substantially large volumes of FDI will flow to India. We list some of the major determinants below:

1. RESTRICTIVE FDI REGIME

The FDI regime in India is still quite restrictive. As a consequence, with regard to cross-border ventures, foreign ownership of between 51 and 100 percent of equity still requires a long procedure of governmental approval baring few sectors. In our view, there does not seem to be any justification for continuing with this rule. This rule should be scrapped in favor of automatic approval for 100 % foreign ownership except on a small list of sectors that may continue to require government authorization. The banking sector, for example, would be an area where India would like to negotiate reciprocal investment rights. Besides, the government also needs to ease the restrictions on FDI outflows by non-financial Indian enterprises so as to allow these enterprises to enter into joint ventures and FDI arrangements in other countries. Further deregulation of FDI in industry and simplification of FDI procedures in infrastructure is called for.

2. LACK OF CLEAR CUT AND TRANSPARENT SECTORAL POLICIES FOR FDI

Expeditious translation of approved FDI into actual investment would require more transparent sectoral policies, and a drastic reduction in time-consuming red-tapism and unauthorized delays by the governmental officials.

3. **HIGH TARIFF RATES BY INTERNATIONAL STANDARDS**

India's tariff rates are still among the highest in the world, and continue to block India's attractiveness as an export platform for labour-intensive manufacturing production. On tariffs and quotas, and on average tariff rate, India is ranked 59 out of 59 countries being ranked. Much greater openness is required which among other things would include further reductions of tariff rates to averages in East Asia (between zero and 20 percent). Most importantly, tariff rates on imported capital goods used for export, and on imported inputs into export production, should be duty free, as has been true for decades in the successful exporting countries of East Asia.

4. **LACK OF DECISION-MAKING AUTHORITY WITH THE STATE GOVERNMENTS**

The reform process so far has mainly concentrated at the central level. India has yet to free up its state governments sufficiently so that they can add much greater dynamism to the reforms. In most key infrastructure areas, the central government remains in control or at least with veto over state actions. Greater freedom to the states will help foster greater competition among themselves. The state governments in India need to be viewed as potential agents of rapid and salutary change. Brazil, China and Russia are examples where regional governments take the lead in pushing reforms and prompting further actions by the central government. In Brazil, it is Sao Paulo and Minais Gerais which are thereform leaders at the regional level; in China, it is the coastal provinces, and the provinces farthest from

ICOQM-10 June 28-30, 2011238 Beijing, in the lead; in Russia, reform leaders in Nizhny Novgorod and in the Russian Far East have been major spurs to reforms at the central level.

5. **LIMITED SCALE OF EXPORT PROCESSING ZONES**

The very modest contributions of India's export processing zones to attracting FDI and overall export development call for a revision of policy. India's export processing zones have lacked dynamism because of several reasons, such as their relatively limited scale; the Government's general ambivalence about attracting FDI; the unclear and changing incentive packages attached to the zones; and the power of the central government in the regulation of the zones, in comparison with the major responsibility of local and provincial government in China. Ironically, while India established her first EPZ in 1965 compared with China's initial efforts in 1980, the Indian EPZs never seemed to take off -- either in attracting investment or in promoting exports.

6. **NO LIBERALIZATION IN EXIT BARRIERS**

While the reforms implemented so far have helped remove the entry barriers, the liberalization of exit barriers has yet to take place. In our view, this is a major deterrent to large volumes of FDI flowing to India. An exit policy needs to be formulated such that firms can enter and exit freely from the market while it would be incorrect to ignore the need and potential merit of certain safeguards, it is also important to recognize that safeguards if wrongly designed and/or poorly enforced would turn into barriers that may adversely affect the health of the firm. The regulatory framework, which is in place does not allow the firms to undertake restructuring.

7. **STRINGENT LABOUR LAWS**

Large firms in India are not allowed to retrench or layoff any workers, or close down the unit without the permission of the state government. While the law was enacted with a view to monitor unfair retrenchment and layoff, in effect it has turned out to be a provision for job security in privately owned large firms. This is very much in line with the job security provided to public sector employees. Most importantly, the continuing barrier to the dismissal of unwanted workers in Indian establishments with 100 or more employees paralyze firms in hiring new workers with regard to labor regulations and hiring and firing practices. Labour-intensive manufacturing exports require competitive and flexible enterprises that can vary their employment according to changes in market demand and changes in technology, so India remains an unattractive base for such production in part because of the continuing obstacles to flexible management of the labour force.

8. FINANCIAL SECTOR REFORMS

Reform of India's financial sector is crucial for large FDI flows into India. However, only some partial steps have been undertaken and these are by no means going to make any meaningful changes to the existing system. India's banking and insurance companies were nationalized more than two decades ago. While a number of countries had undertaken such actions in the 1970s and early 1980s, for instance Mexico, France, and Chile, however, they have almost completely reversed this policy by now. Be that as it may, India still continues to rely on a state-owned, state-run banking system and the expect has had highly adverse results, both in terms of availability of funds for investment and a negligible presence of foreign banks and least presence of foreign insurance companies in the country.

9. HIGH CORPORATE TAX RATES

Corporate tax rates in East Asia are generally in the range of 15 to 30 %, compared with a rate of 48 % for foreign companies in India. High corporate tax rate is definitely a major disincentive to foreign corporate investment in India.

10. FLUCTUATING EXCHANGE RATES

The exchange rates of different currencies are very much fluctuating time and again which poses problem for the prospective investor in the country. The past trends were not satisfactory, hopes to improve in future No doubt the fluctuation were temporary but it has affected the inflow of FDI to a large Extent in India and other Asian countries.

11. **INDECISIVE GOVERNMENT AND POLITICAL INSTABILITY**

There was to many anomalies on the government side during past two decade which is still affecting the direct inflow of FDI in India such as mismanagement and oppression by the different company,which affect the image of the country and also deject the prospective investor, who are very much conscious about safety and constant return on their investment.

SECTION- V

CONCLUSIONS

The study shows that India’s share in world Foreign Direct Investment (FDI) rose to 2.44% in 2008 as compared to 0.09% in 1991. This can be attributed to economic reform process of the country. There has been a generous flow of FDI in India since 1991 and its overall direction remained the same over the years irrespective of the ruling party. A comparative analysis of FDI approvals and inflows reveals that there is a huge gap between the FDI amount approvals and inflows reveals that there is a huge gap between the amount of FDI approved and its realization into actual disbursements in India. India received large amount of FDI from Mauritius (nearly 40% of the total FDI inflows apart from U.S.A (8%), U.K (6.1%). The empirical results of Determinants of FDI inflows in India shows that GDP , trade openness and Inflation exhibit a positive relationship with FDI while Foreign Exchange Reserves exhibit a negative relationship with FDI inflows in the country during the period 1992-93 to 2008-09. It is observed that major FDI inflows in India are concluded through automatic route and acquisition of existing shares than through FIPB, SIA route during 1991-2008.

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