

# Determinants of Foreign Direct Investment in India

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## Abstract

Tamil Nadu wears the most urbanized state of India. Its manufacturing sector is well developed and factories in the country are also the most numerous in India, and the population of skilled workers in it is also the greatest. It has been in the lead, in the fields of automotive, engineering, research and development, health care, IT and IT enabled services, textiles, cotton, field, financial and leather industries. It is also one of the top destinations in India in terms of foreign direct investment as it records 7 percent of the total foreign direct investment made in India between 2011-2021. The state has also accommodation of manufacturing facilities of over 50 fortune 500 companies and is the top destination of Japanese and Korean investments in India. It has one of the leading automotive centers in its capital Chennai. Tamil Nadu is leading investment destination in India to the foreign investors on account of its developed infrastructure and network capability as also locational incentive which serves its already developed manufacturing eco system and exports too. The economy of Tamil Nadu revolves around the service industry, manufacturing industry as well as the agricultural sector. Totals of direct investments brought about by foreign investments to the state stand at 14.9 percent. Tamil Nadu registers the second-best nominal gross state domestic product in India with US \$260 billion in 2019-2020. Majorly in this paper attention will be paid to the various sectors FDI inflows in India that comprise of Manufacturing, Construction, Financial Services, Miscellaneous, Retail and Wholesale trade, Telecommunication. Thus, an effort is made to determine the FDI inflows determinants in India in the past decade between 2011-12 and 2020-2021. Growth rate was also used by the researcher to ascertain the increments or declines of FDI in different sectors over the recent decade.

**Keywords:** *Foreign Direct Investment, Investment, Sectors*

## Introduction

The policies of foreign direct investments contribute significantly to economy of developing nations within the globe. Shifting towards conducive policies to draw FDI inflow has now turned out to be a major battle ground in the emerging economies. The role of foreign direct investment has been complementary in the general capital formation and in curbing the gap between the domestic savings and investment. The non debt creating source of additional external finances especially at the macro level is foreign direct investment; FDI would enhance the policy makers level of national income and output. On the micro level, foreign direct investment is expected to have a bearing in terms of the effectiveness of the technical effectiveness and administration effectiveness of the joint ventures, enhancement of the skill levels due to labour training of the local firms via the technology transfer and spillover effects. Foreign direct investment is manifested in India in terms of development tool and

this has helped in achieving self-reliance in different areas in addition to supporting inclusive growth of the economy. India, just like many other developing countries had mainly followed inward looking growth policy of import substitution coupled with a limiting FDI policy.

The economy of India is growing at a fast rate and foreign direct investment (FDI) is coming to India to get an increment in their domestic investments and attain new management and technologies. Promotion of foreign direct investment (FDI) is also a significant constituent of the economic change that is occurring in India currently. The majority of strategies of attracting foreign direct investment (FDI) is the result of the signs that the number of measures to stimulate foreign investment (FDI) is required and will result in the growth of investments. As UNCTAD (United Nations conference on Trade & Development -World investment report 2020) indicates, India is in the 9<sup>th</sup> position of top ten countries attracting FDI. The Reserve bank of India recent Annual report as on 2020-21 has shown that the total amount of foreign direct investment in India is US \$ Million 52,545.

### **Review of Literature**

In their research titled A study on Growth of Foreign Direct Investment in the different sectors of Indian Economy A descriptive and Analytical study Ghousia Khatoon (2016) has studied the various objectives of the study that are namely the main objectives of the study is to analyze the country wise inflows of FDI in India. The scholar came to the conclusion that FDI is of crucial significance to an Indian economy because it will not only result in capital formation but also employment, transfer of technology, improvement in living conditions, exposure to international pool of managerial skills, optimal use of human resources and the natural resources, the quality of the resources of all kinds available in the world etc.

According to Yilmaz Bayar (2018) in their paper based on the same topic of their research, Foreign Direct Investment (FDI) inflows into the globalized world have increased a lot since the mid-1980s. In his research his main aim is to investigate the relations via panel data analysis of the inflow of FDI and the financial industry growth development in the Central and Eastern European Union countries in the period 1996-2015. The finding of the researcher indicates that a co- integrating relationship does not exist between FDI inflows, foreign portfolio investments, and development of the financial sector but financial development influences short-term FDI inflows in a one-way direction.

In carrying out his research, M. Kanaga, K. Uthayasuriyan (2019) noted that his study was to examine the FDI flows country wise in IT sector as there has not been a study in this regard in the past. Based on his findings it is perceived that the major positive trend contribution of IT Sectors inflow is 2487 million in 2017-18 and 2361.8 million in 2016-17. The minimum value of trends of inflows is 2013-14 which is 1983.6million. The researcher indicated that the government had to come up with mechanisms that would make the manufacturing sector more appealing to the foreign investment as compared with the IT industry. The FDI policy in India has also been liberalized in an attempt to attract investors in the country. The country is regularly ranked among the top three investment locations in the world by all international organizations as is the case in the current circumstances.

### **Objective of the Study**

The main objective of the study is to analyse the determinants of foreign direct investment in India.

### **Data Analysis and Interpretation**

FDI policy is an enabling policy which is uniformly applicable in the country. Government has put in place a liberal and transparent policy for Foreign Direct Investment (FDI), wherein most of the sectors are open to FDI under the automatic route. The Government reviews the FDI policy and makes changes from time to time, to ensure that India remains an attractive & investor friendly destination.

Make in India initiative was launched with the objective of facilitating investment, fostering innovation, building good quality manufacturing infrastructure, making it easy to do business and enhancing skill development. The initiative is further aimed at creating a conducive environment for investment, modern and efficient infrastructure, opening up new sectors for foreign investment and forging a partnership between government and industry through positive mindset. FDI policy is a facilitating policy and it is applied consistently in the country. A liberal, transparent policy has been put in place on Foreign Direct Investment (FDI) whereby, the Foreign Direct Investment under automatic route is open in most of the sectors. The FDI policy is reviewed by the Government every now and then and alterations are made to take into consideration that India is an attractive destination and also investor friendly. Make in India program was introduced with the aim of streamlining investments, promotion innovation, development of good quality of manufacturing infrastructure, simplifying business environment and promoting skill development. The initiative is also geared towards having a favorable investment climate, constructive and productive infrastructure, new areas to be opened up to foreign investment and establishment of symbiotic relationship between the industry and the government where good attitude prevails.

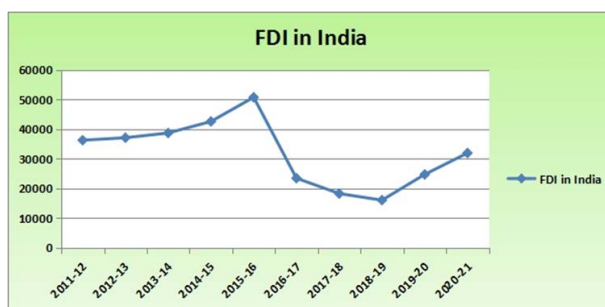
### Gross Inflows of Foreign Direct Investment in India from 2011 to 2021

The gross inflow of Foreign Direct Investment in India from 2011 to 2021 were given in below table 1.

**Table 1 Gross Inflows of Foreign Direct Investment in India from 2011 to 2021 (US\$ million)**

Year	FDI in India	Increase/ Decrease	GR %
2011-12	36306	-	-
2012-13	37140	834	2.29
2013-14	38745	1605	4.32
2014-15	42630	3885	10.02
2015-16	50800	8170	19.16
2016-17	23473	-27327	-53.7
2017-18	18286	-5187	-22.0
2018-19	16054	-2232	-12.20
2019-20	24748	8694	54.15
2020-21	31978	7230	29.21
Minimum	16054		
Maximum	50800		
Mean	32016		
Standard Deviation	11178.6		
CAGR	-11.92		

Source: Reserve Bank of India, Annual Report



**Figure 1 Gross Inflows of Foreign Direct Investment in India from 2011 to 2021**

The inflow of Foreign Direct Investment in India in dollar terms has reduced between the years 2011-12 and 2020-21 to touch the figure of \$31978 million. Trends of the Foreign Investment inflows to India indicates that it is rising by the year except in few instances. The maximum annual rate of growth viz. 54.15 per cent was observed in the year 2019-20 and the minimum annual growth rate viz. -53.7 per cent was observed in the year 2016-17. The negative growth rate is realized in some of the years in the study periods.

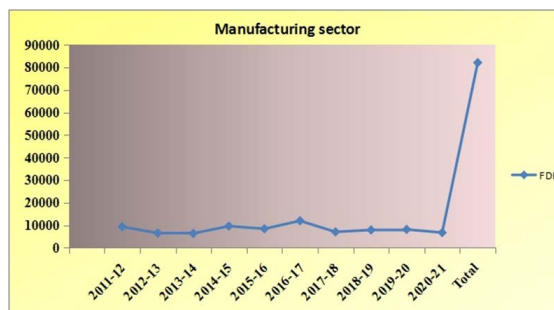
#### Foreign Direct Investment Inflows in India - Manufacturing Sector

The economic growth and development of India has been greatly attributable to manufacturing. In the recent two years government of India has made a number of reforms and steps to improve manufacturing industry in India. Between April 2000 to December 2020, the amount of Foreign Direct Investment in India manufacturing sector is USD 89.15 billion. In a further attempt to promote FDI, recently in Sep 2020 government of India reduced the base corporate tax to 15 percent to 25 percent in the manufacturing sector in new companies.

**Table 2 Foreign Direct Investment Inflows In India - Manufacturing Sector (US\$ million)**

Year	FDI in Manufacturing sector	Increase/ Decrease	GR %
2011-12	9,337	-	--
2012-13	6,528	-2809	-30.08
2013-14	6,381	-147	-2.25
2014-15	9,613	3232	50.6
2015-16	8,439	-1174	-12.21
2016-17	11,972	3533	41.86
2017-18	7066	-4906	-40.97
2018-19	7919	853	12.07
2019-20	8153	234	2.95
2020-21	6739	-1414	-17.3
Minimum	6,381		
Maximum	11,972		
Mean	8214.7		
Standard Deviation	1737.76		
CAGR	-3.20		

Source: Reserve Bank of India, Annual Report.



**Figure 2 Foreign Direct Investment Inflows In India - Manufacturing Sector**

As it is seen in the above table 1.2 it can be stated that the FDI inflow in India has increased between the year 2011 and 2021. The inflow of FDI in India was 9,337 million in the year 2011-12 and it steadily declined between the years 2012 and 2014 and the figure stood at 6,381 during 2011-12. In the year of 2016-17 again it has risen up to 11, 972 million and again in the year of 2020-21 there is again a decrease of 6739 million. The FDI inflow increases at a positive rate of growth in the year 2014-15 and 2016-17 in India. The annual growth rate viz. 50.6 per cent was highest in the year 2014-15 and the lowest annual growth rate viz- 40.97 per cent was during the year 2017-18. The negative growth rate occurs in some of the years under the study periods.

### Foreign Direct Investment Inflows in India- Miscellaneous Services

The foreign direct investment in miscellaneous services in India were given in below table 3

**Table 3 Foreign Direct Investment Inflows in India- Miscellaneous Services (US\$ million)**

Year	FDI in Manufacturing sector	Increase/ Decrease	GR %
2011-12	801	-	-
2012-13	552	-249	-31.08
2013-14	941	389	70.4
2014-15	586	-355	-37.72
2015-16	1022	436	74.4
2016-17	1816	794	77.6
2017-18	835	-981	-54.01
2018-19	1226	391	46.82
2019-20	443	-783	-63.8
2020-21	671	228	51.4
Minimum	443		
Maximum	1816		
Mean	889.3		
Standard Deviation	402.1841		
CAGR	-1.75		

Source: Reserve Bank of India, Annual Report.



**Figure 3 Foreign Direct Investment Inflows in India – Miscellaneous Services**

Looking at the table 3, the figures record the gross inflows of the Foreign Direct Investment in miscellaneous services between 2011 and 2021. The flow of a Foreign Direct Investment to India is 801 million in the year 2011-12 and it had a slow increase until the year 2016-17 which is 1816 million. FDI inflow of India shows positive indicators of growth rates in miscellaneous service in the year 2013-14, 2015-16, 2016-17, 2018-19 and 2020-21. The maximum and the minimum growth rate of the year is viz. 77.6 per cent and -63.8 per cent in the year 2016-17 and the year 2019-20 respectively. The negative growth rate is shown in the study in certain periods of the years under study.

### Foreign Direct Investment Inflows in India - Retail and Whole Sale Trade

India has adopted liberal position in so far as the extent of permitted FDI is concerned registered as cash and carry wholesale trade, B2B (Business to Business) trade, single brand goods etc., foreign direct investment in retail trade with single brand goods has not been permitted. In the retails sector, the protection of India against the organized retailing, which is traditionally unorganized, is the main motive of restricting the foreign direct investment.

**Table 4 Foreign Direct Investment Inflows in India- Retail and wholesale trade (US\$ million)**

Year	FDI in Retail & Wholesale trade	Increase/ Decrease	GR %
2011-12	567	-	-
2012-13	551	-16	-2.821
2013-14	1139	588	106.7
2014-15	2551	1412	123.96
2015-16	3998	1447	56.722
2016-17	2771	-1227	-30.69
2017-18	4478	1707	61.60
2018-19	4311	-167	-3.729
2019-20	4914	603	13.987
2020-21	2960	-1954	-39.76
Minimum	551		
Maximum	4914		
Mean	2824		
Standard Deviation	1629.209		
CAGR	17.96		

Source: Reserve Bank of India, Annual Report.



**Figure 4 Foreign Direct Investment Inflows in India – Retail and wholesale trade**

One can find in the table 4 the gross inflows of the Foreign Direct Investment in the retail and wholesale trade between 2011 and 2021. The inflow of a Foreign Direct Investment in India stands at a figure of \$567million in the year 2011-12 and since then, the down was in an ascending trend in the year 2015-2016, to a value of \$3998million. However, at the same time it has fallen to 2771 million in the current year 2016-17. Again it has been surged up Rs.4914 million in the year 2019-20. Inflow FDI in India has an upward growth rate in the retail and the wholesale trades in 2013-14 to 2015-16, 2017-18 and 2019-20. The maximum and minimum annual growth rate were observed in the year 2014-15 and the year 2020-21 with the rate of 123.96 per cent and -39.76 per cent respectively. During some of the years in periods of study show the negative growth rate.

## Conclusion

FDI policy is enabling policy and it applies equally in the nation. A liberal and transparent policy has been developed by Government on Foreign Direct Investment (FDI) whereby majority of the sectors are FDI rich under the automatic route of FDI. The Government considers the policy on FDI and amends it at various times, so that India continues to be an attractor & a friendly destination to the investors. The idea behind introducing Make in India initiative was to enable investment, promote innovation, develop good quality manufacturing infrastructure, make it easy to do business and how skill development would work. The scheme will also work towards providing an ideal environment of investment, modern and efficient infrastructure, opening up of other sectors to foreign investments as well as establishment of harmony between the government and industry through positive thinking.

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