FDI Flows in Developing Countries: An Empirical Study

Azeem Ahmad khan

Department of commerce, Aligarh Muslim University
Aligarh, UttarPradesh, India-202002
E-mail: azeemgc7011@gmail.com

Abstract. In this research paper, an effort has been made to evaluate the FDI flows in India through Mergers and Acquisitions, a composite view of effective practices that have been emerged from inbound investors’ experience conducting M&As in India. However, a number of successful deals shortlisted based on their size and prominence in the Indian market. Foreign Direct investment is a subject of interest in India. The World Bank is an international financial institution that provides loans to developing countries for capital programme. The countries of the world, particularly developing economies, are rivals to attract foreign capital to boost their domestic rates of investment and also to acquire new technology and managerial skills. The wave of liberalization and globalization sweeping across the world has unlocked many national markets for international business. It is stated that FDI has to play a vital role in the existing world economy. Therefore Cross border merger and acquisitions have emerged as the single largest way of integrating the world economies on the basis of investment done way back where they accounted majority of FDI flows.

Key Words: FDI, Inbound, Outbound, World Bank and Mergers and Acquisitions.

1. Introduction
In today’s world, foreign direct investment (FDI) as a strategic component of investment and is a need for India to achieve the economic reforms and to maintain the pace of growth and development of the economy. FDI is considered to be the most attractive type of capital flows for emerging economies as it is expect to bring latest technology and enhance production capabilities of the economy. The rate of FDI inflow in India was initially low due to regulatory policy framework but there is a sharp rise in investment from 2005 towards because of the new policy [1]. The country has seen major global economic crises, a succession of coalition governments, an IT
and outsourcing revolution and further fragmentation of its political landscape. During this period, India has remained open for business and has offered opportunities to global companies who have bet on its growth story. Despite the turbulence from 2008 global financial crisis and recent policy uncertainty, India’s long term drivers have remained attractive for international companies. Its growth of middle class consumers will continue to attract both at first-time, as well as in serial acquirers of more companies looking to capture a piece of the market which increases the FDI flows in India. (See in Figure1). The road to foreign direct investment (FDI) recovery is bumpy. Global FDI fell by 18 per cent to $1.35 trillion in 2012. But India’s FDI inflows have increased from 3.3 billion $ in 2001 to 19.8 billion $ in 2013. The recovery will take longer than expected, mostly because of global economic fragility and policy uncertainty. Foreign direct investment in India has increased 35 per cent to USD 13.6 billion during the first half of 2013 with merger and acquisitions accounting for the bulk of inflows, says an UNCTAD report. In the beginning of 2014, India has not seen negative FDI flows for Q1 FY14 net FDI inflows were $ 6.5 billion. Foreign direct investment refers to building new facilities, reinvesting profits earned from overseas operations and intra company loans. So Mergers and acquisitions is a successful strategy for investment. KPMG (Klynveld Peat Marwick Goerdele) report brings together unique insights and experiences of global acquirers who have successfully conducted M&As in India over the last six years, including what they have learned from the process and their effective practices that resulted in a successful deal. Moreover Cross-border mergers and acquisitions (M&As) and large retained earnings kept in foreign affiliates were driving forces behind the current global

**Figure 1:** Exhibit the FDI trend in India over the years in US $ Billion.

![Graph](https://placehold.it/200)

*Source: RBI*

FDI growth, rather than investment in new productive assets through Greenfield investment projects, so FDI is on the rise in structurally weak economies. As a result, inbound M&As has seen more deal activity than both domestic and outbound M&As for a majority of the past decade. (See in figure 2)
Figure 2: Shows the Indian M&As Volume in respect of Inbound, Outbound and Domestic Mergers and Acquisitions.

Source: Merger Market

2. Review of Literature

Nayak, Ranjan Kumar (2013)[ix] has examined the growth patterns and changing nature of Indian inward Foreign Direct Investment, with an emphasis on the post liberalization period, since FDI, along with trade, has been an important mechanism which was brought about a greater integration of Indian economy with world economy. Goel, Shashank., et al., (2012) [i] examined in their paper that foreign Direct Investment Model reveal that Trade GDP, Reserves GDP, and financial Position variables exhibit a positive relationship with FDI while R&D GDP and Exchange rate variables exhibit a negative relationship with FDI inflows. Singh Y., Bhatnagar A. (2011) [x] found after the comparative analysis of FDI in India and china that both enjoy healthy rates of economic growth but FDI inflow in china is higher than India. Khan A.Q. and Siddiqui Ahmad Taufeeque (2011) [xi] studied the impact of FDI on Indian economy and a comparison with China & USA. The paper has also been ventured into carving out set of strategies to deal with the issues & problems in attracting FDI for promotion & growth of international trade. The double log model has been used to find elasticity between different factors in this paper. They also highlight the impact of FDI on employment. In this research paper, the discussion between FDI and GDP as to asses that FDI helps in boosting growth of a country. Bhanagade D.B, Shah A. Pallavi (2011)[xii] examined in their paper that the impact of FDI on Indian Economy where they also emphasize on the investments, sectors attracting highest FDI inflows and FDI leads to Generation of Employment opportunities. Therefore the growth of inflow of FDI would lead to positive growth of Gross capital formation. In India, the growth of GDP is largely influenced by FDI. Chaturvedi Ila (2011) [xiii] in his paper, analyze the FDI inflows with special reference to sector wise inflows in India. This paper also explore the sector wise distribution of FDI in order to know the dominating sector which has attracted the major share of
FDI in India. And to find out the correlation between FDI and Economic Development, it reveals that there is high degree of significance between FDI and economic development. Agarwal G., and Khan M. A. (2011) \[^{xv}\] analyzed the Impact of FDI on GDP through Comparative Study of China and India and they found that 1% increase in FDI would result in 0.07% increase in GDP of China and 0.02% increase in GDP of India. We also found that China growth is more affected by FDI, than India’s growth. Singh S., Singh M. (2011) \[^{xvi}\] they examined the trend of FDI inflow to India, during 1970–2007 using time series data. Singh J. (2010) \[^{xvii}\] analyzed Economic Reforms and Foreign Direct Investment in Indian Policy, Trends and Patterns in the context of increasing competition among nations and sub national entities to attract Foreign Direct Investment (FDI) and suggest that the FDI inflows, in general, show an increasing trend during the post-reform period.

3. Research Gap
It is seen that, most of the works have been done on trends, policies, issues, challenges and their structural framework, while aspect FDI through Mergers & Acquisitions in India have not give due importance, which is needed to be investigated. The present study would go to investigate the detail of FDI with greater focus on the developing nation India. The study will also discuss the FDI which comes through Equity Capital of Unincorporated Bodies. An attempt is made to insight the present scenario of FDI in India on the basis of Inflows and relationship with gross domestic product (GDP) of India.

4. Objectives of the study
   - To examine the relationship between FDI through FIPB /Acquisitions Route and total FDI in India.
   - To examine the relation between FDI inflows (Inward) and GDP of India.
   - To study the difference between FDI through FIPB /Acquisitions Route and Equity Capital of Unincorporated Bodies.

5. Hypotheses of the Study
The Hypotheses investigated in the study are listed below:
   - H\(_{1_0}\) – There is no significant relation between FDI through FIPB /Acquisitions Route and total FDI in India.
   - H\(_{2_0}\) – There is no significant relation between FDI inflows (Inward) and GDP of India.
   - H\(_{3_0}\) – There is no significant difference between FDI through FIPB /Acquisitions Route and Equity Capital of Unincorporated Bodies.

6. Methodology of the study
This study has been carried out with the help of secondary data only, all the data has been collected from the various sources and compiled as said by the need of the study. The major sources includes World Bank, UNCTAD, RBI bulletins, annual reports and handbook of statistics on Indian economy, Department of Industrial Policy and
Promotion (DIPP), SIA newsletter, books, journals and the like. For analyzing the relationship between FDI through FIPB /Acquisitions Route and total FDI and FDI inflows (Inward) and GDP in India used Correlation and Regression in addition to find out the difference between FDI through FIPB /Acquisitions Route and Equity Capital of Unincorporated Bodies applying t-test.

7. Analyses and Interpretations

**Hypothesis-I** The relationship between FDI through FIPB /Acquisitions Route and total FDI in India defined the correlation coefficient \((r)\) is 0.991 which is a very high degree of positive correlation. The coefficient of determination \((r^2)\) is 0.982 indicating that 98.2 percent of variance is explained by this relationship. The regression equation \(Y\) on \(X\) shows that every unit change in \(X\) that is FDI through FIPB /Acquisitions Route in India there is 1.368 units change in \(Y\) that Total FDI in India. The Intercept value is 1823.293 indicating the role of other factors. The \(t\)-value is 25.458 for 14 years of data undertaken for the analysis and also indicates the \(p\)-value is 0.000 which is less than 0.05 which leads to significant statistically, hence there is significant relation between FDI through FIPB /Acquisitions Route and total FDI in India.

**Hypothesis-II** The relationship between GDP of India and FDI flows (Inward) in India defined the correlation coefficient \((r)\) is 0.241 which is a low degree of positive correlation. The coefficient of determination \((r^2)\) is 0.058 indicating that 5.8 percent of variance is explained by this relationship. The regression equation \(Y\) on \(X\) shows that every unit changes in \(X\) that is FDI flows (Inward) in India there is 6.454 units change in \(Y\) that is GDP of India. The Intercept value is 5.026 indicating the role of other factors. The \(t\)-value is 1.587 for 43 years of data undertaken for the analysis and also indicates the \(p\)-value is 0.120 which is more than 0.05 which leads to statistically insignificant, hence there is no significant relation between FDI inflows (Inward) and GDP of India.

**Hypothesis-III** This hypothesis examines the difference between FDI through FIPB /Acquisitions Route and Equity Capital of Unincorporated Bodies, the mean of FDI through FIPB /Acquisitions Route is 15108.9286 and for the Equity Capital of Unincorporated Bodies the mean is 751.6429 when undertakes the fourteen year data used. The standard deviation for the FDI through FIPB /Acquisitions Route is 11715.85731 and for the Equity Capital of Unincorporated Bodies had 618.58046 and the mean difference was 14357.28571. The \(t\)-statistics is 4.761 along with the \(p\)-value is 0.000 which is less than 0.05 which leads to the conclusion that the difference is statistically significant. Therefore the Null Hypothesis is rejected. Hence it is concluded that there is significant difference between FDI through FIPB /Acquisitions Route and Equity Capital of Unincorporated Bodies.

8. Conclusion

This empirical study suggests that FDI has a beneficial impact on developing countries but recent work also points out some potential risk. Mergers & Acquisitions help in increasing the FDI inflows in India, the result of the study shows that the large amount of FDI comes through Mergers and Acquisitions in India. However the
relationship between FDI inflows (Inward) and GDP of India are not significant for the reason that they fail to attract the foreign Investors. But the difference between FDI through FIPB /Acquisitions Route and Equity Capital of Unincorporated Bodies statistically significant and leads to conclusion that other sources of Investment rather than Mergers and Acquisitions are least effective and still efforts are require for attracting foreign Investors.

**References**


[5] Ibid, pp-70


