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THE ROLE OF FDI IN ENHANCING FINANCIAL STABILITY IN EMERGING MARKETS

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Abstract

FDI is the term for capital inflows from abroad that are used to enhance or increase the potential for economic growth. The connection between FDI and economic growth has garnered a lot of interest in the study of global growth for a while now. In a time of unsure global capital progressions, foreign direct investment (FDI) emerges as a workable detour to more rapid growth in developing nations. It plays a significant role in the long-term development of a nation as a source of capital and for enhancing the seriousness of the domestic economy through initiatives toward innovation, supporting the legal system, increasing efficiency, and opening up new business opportunities. Foreign direct investments (FDI), which are permitted across industries and business sectors, have steadily increased, demonstrating the faith that international financial backers have in the flexibility of Indian markets. The data also reveals a high correlation between the increase of FDI and GDP and that the flow of FDI into India is positively impacting the country's GDP. The expansion of FDI and FII provides additional evidence of this positive relationship.

Keywords: *FDI, Foreign Direct Investment, Enhancing Financial Stability, Emerging Markets*

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1. Introduction

A venture operating in a nation with a distinct economy is referred to as receiving a "foreign investment" if net capital inflows are made in exchange for a lasting management premium, which is defined as 10% or more of the voting stock. This is the sum of value capital, earnings reinvestment, other long-term capital and short-term capital at an interest rate yet to be determined. It often comprises of managerial support, collaborative efforts, innovative actions, and skill. Direct investing avoids investment by accepting offers. FDI is one illustration of a worldwide variable development. a foreign investment that often imposes constraints on the group that it is funding. The simplest definition of FDI would be a partnership's direct investment in an international business enterprise. It is essential to distinguish this activity from participation in other undertakings in a foreign country by demonstrating that the business venture works totally outside the economy of the organization's country of origin.

In non-industrialized nations, academics and lawmakers have given the connection between FDI and economic growth a lot of thought. Since one of these countries' main objectives is economic expansion, FDI-related initiatives have received attention as these countries' economies have developed and flourished. It is widely acknowledged that FDI fosters innovation, which is utilized to develop labour and products, and lessens the difficulty of saving and investing. Additionally, FDI increases money and human resources. From another perspective, it is very plausible to argue that foreign direct investment is one of the key factors in the process of economic integration, as it enhances benefits and long-term partnerships between different nations.

Researchers have talked about the many beneficial effects that FDI can have on the economy. In addition to diversifying the capital structure of beneficiaries, FDI also has positive externalities such as innovation and knowledge transfer. For example, foreign direct investment increases investment, thereby offsetting the investment-saving imbalance. However, previous studies have shown that foreign direct investment has a negative impact on economic growth in the short term, but a positive one in the long term.

In an era of globalization where economic, commercial and technological barriers are becoming increasingly unclear, emerging markets value foreign direct investment as a positive effect. Even if each nation has particular strengths and resources that it can employ to develop

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its economy, FDI is one of the main elements that directly affect growth. Through FDI, which also encourages financial stability, economic advancement, and cooperative government aid, it is possible to establish global economic harmony.

While it could well be argued that foreign direct investment (FDI) could bring extraordinary benefits to wealthy countries, Harvard Business College's Laura Alfaro notes that an April 2003 report on FDI and the economy A study on growth found that the benefits of FDI vary greatly from country to country industry. She specifically looked at how FDI affected the growth of the manufacturing, services, and essential goods sectors. A thorough examination of cross-country statistics from 1981 to 1999 reveals that total FDI has a small impact on growth. However, foreign direct investments frequently have a detrimental effect on growth, whereas investments in assembling have a positive effect. It's unclear whether the assistance section can offer evidence.

2. Literature Review

Since the mid-1990s, when foreign investments were viewed as only being in created nations and the other nations were denied of this chance to benefit from the foreign assets to help up their economic strength, Philippe Bacchetta (2000) has completely covered the important parts of the foreign direct investments in emerging markets. He starts from the verifiable foundation of foreign direct investments. This notion that investments should be made in created nations should be as it were started to alter not long after the financial turbulence. Many multinational corporations realized that a healthy economy wasn't the only place where they could increase their profits and spur company growth; emerging economies also offered fantastic opportunities for multinational corporations to increase their profits, win over the patronage of their clients, and expand and grow their operations.

According to Silvio Contessi and Ariel Weinberger (2009), Asia and Latin America receive the greatest amount of foreign direct investments relative to the rest of the world. Due to their abundance of conventional assets, sizable markets, and potential of gaining additional customers, all international businesses typically invest in these mainlands.

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According to Marianne Ganster (2007), several countries in Asia and Latin America have amazing geographical features that attract tourists. Some of these countries also have ocean ports and ocean routes that make it easier to import and export goods. She also reiterates that land developments are completely useful in many different countries. Financial backers would typically invest resources in a variety of projects because the likelihood of failure is so remote.

Amal, M. (2011) has also described the models used to choose the country where a company should launch the venture. The organizations may have two concerns; some companies are more concerned with the economic and political conditions of the host countries prior to making investments, while others are more concerned with the competitors' visibility and market capturing. Each company has a different preference when deciding where to give, and the decision may alter over time. Report on the Capital Market Counseling's working meeting Gathering ensures that a company can choose among the several types of foreign direct investments, including whether to invest in a joint venture, buy an existing company (acquiring), or start a brand-new venture. When businesses enter a country in an intriguing way and learn all there is to know about it—its laws and clients' concerns—they frequently prefer joint ventures before switching to green field investments.

According to Christopher Kramer (2010), there are four factors that a corporation considers while making investment decisions. Most importantly, the company must research the resources and assets that are available to it in order to launch a new project. If the resources have a positive net present value, the company must also research the market in which the new project will be implemented. The company can imagine tolerating the venture as long as the cost is fair and does not quite match the anticipated returns. The third factor that needs to be kept in mind is the location advantage. If a company is located far from the market, a competitor may take advantage of early product delivery, and the cost of transportation will also increase because of how far the manufacturing facility is from wholesalers and retailers. If all of these requirements are satisfied, the company must determine if the endeavor will help it achieve its long-term objectives or not. Benefits are not always desirable, as seen in projects like the ventures started by governments and social workers who are committed to the welfare of humanity rather than their own financial gain. In this method, the company should choose the project if it aids in achieving the company's goals, and the financial backers will make such foreign direct investments.

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3. Routes of FDI in Indian companies

Under the two courses offered under "Foreign Direct Investment," an Indian organization could receive:

1) Automatic Route: Without prior approval from the Public Authority of India or the Hold Bank of India, FDI is permitted under the scheduled course in movements of all kinds and areas as established by the United FDI Strategy, which is occasionally provided by the Public Authority of India.

2) Government Route: For foreign direct investment in exercises not covered by the planned course, the Ministry of Economy and Finance's Foreign Investment Promotion Board (FIPB) expects prior approval from public authorities.

4. Objective of the Study

1. To examine the FDI trend in India.

2. To examine how FDI and FII interact in India.

3. To examine the connection between FDI and economic growth.

5. Research Methodology

The use of optional information has focused on the aforementioned goals. The supplemental data was acquired from a variety of optional sources, including distributed reports from the World Bank, IMF, World Bank Branch of Industry Strategy and Advancement, and others. Tables and graphs have been used to analyse the information gathered. A straight connection study has been completed to understand the relationship between foreign institutional investment flows, gross domestic product and foreign direct investment flows in India.

6. Data Analysis

From 2000 to June 2014, India received USD 335,020 in Foreign Direct Investment (FDI) for a total of USD 224,817 million. Since 2004, foreign direct investment in India has recorded a significant increase.

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FDI inflows from April 2000 to June 2014 overall

1. The total amount of FDI is US $335020 million.

2. The total amount of FDI inflow was US$ 224817 million.

- **FDI Inflow Year wise**

Table 1: analysing the FDI influx to India, year by year

Year	Total FDI (US $ Million)	Percentage growth over previous year	Investment by FII (US $ Million)
2000-01	3018	********	2736
2001-02	5240	63%	1404
2002-03	4024	(-) 17%	266
2003-04	3411	(-) 15%	10829
2004-05	5042	30%	7575
2005-06	9852	37%	8835
2006-07	12717	257%	4414
2007-08	25752	42%	10437
2008-09	52782	30%	-24026
2009-10	26654	(-) 20%	38057
2010-11	25658	(-) 7%	35533
2011-12	57447	43%	25723
2012-13	43189	(-) 35%	36473
2013-14	25485	7%	6020
2014-15*	7022	********	

6.1. Correlation Coefficient for Karl Pearson

According to the information in Table 1, the total absolute amount of FDI into India and FII investment into India from 2001 to 2014 is 0.330705. The results of this analysis show an imprecise positive correlation between the two criteria. However, data reveals that increased FDI investment in India will lead to an increase in FDI as it has a positive impact on the country's economic development.

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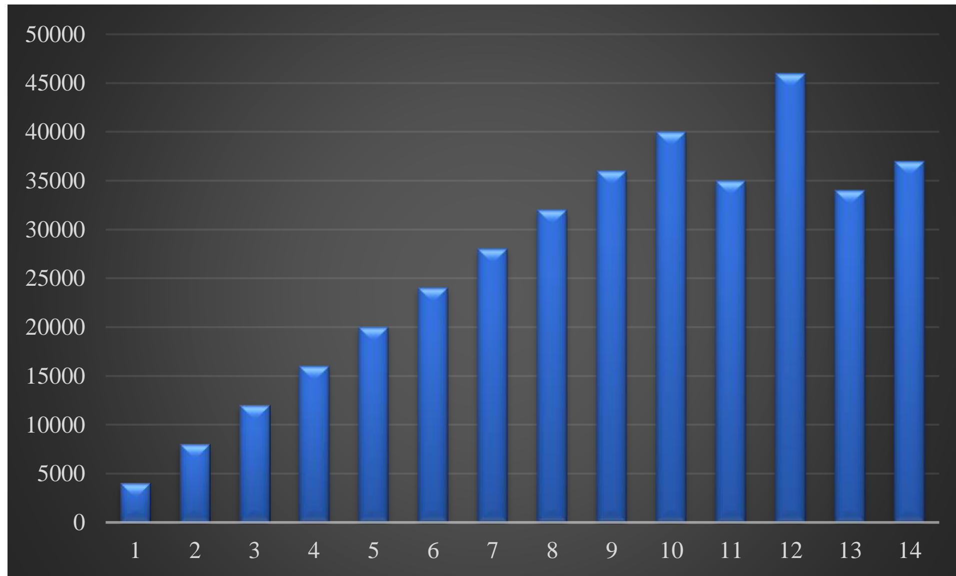

Figure 1: Investment by FIIs and total FDI in India

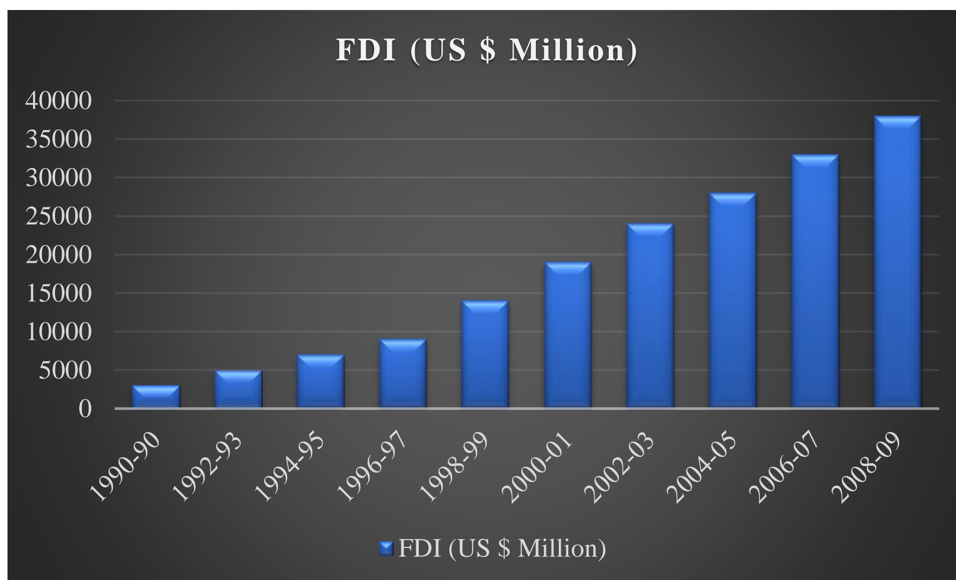

Figure 2: Foreign direct investment trends in India from 1990–1991 to 2009–2010

6.2. The Analysis of Trends

According to the FDI data from 2001 to 2014, FDI into India has typically followed a normal, positive trajectory. However, if we carefully examine the data, starting in 2009 and continuing through 2014, we will discover that India's FDI stream has grown recently. The Indian

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economy began drawing a lot of FDI after 2004. The FDI stream only had a consistent pattern prior to 2004, ranging from US$4029 to US$4322. The dramatic rise in FDI inflows into India was a result of both the capital market's gradual opening up and the economy's expansion beginning in the middle of the 1990s. FDI in India was largely allowed in every sector of the economy as a result of the capital record progression, with a few limitations based on crucial importance and in compliance with the rules and laws for certain fields. According to the data presented above, the majority of the countries experienced a significant decline in the growth of FDI between 2008 and 2010, but India experienced a more moderate decline in FDI as a result of the country's robust value streams, which supported its domestic growth prior to the global recovery, and its consistent reinvestment of profits, which demonstrated higher productivity of foreign companies in India.

The 2012 Reality Investment Report from the Joined Countries Gathering on Exchange and Improvement (UNCTAD) revealed that FDI levels in 2011 were higher than they were prior to the financial crisis. More significantly, the study placed India behind China and the US as the third most popular economy for FDI.

The thorough analysis looked at more than 179 organizations, and it was found that the top 3 nations that welcomed foreign direct investment in 2011 remained stable when compared to the prior year. India was still ranked third overall and second among Developing and Developing Economies, only behind China. In that location over the following three years is predicted to be India.

Table 2: Sectors Bringing in the Most FDI to India (in Crore)

S.NO.	Sector	April 2000-2014	Percentage (%)
1.	Service Sector	298.882	27
2.	Construction and development	120.345	22
3.	Telecommunication	87482	8
4.	Computer software and hardware	70402	7
5.	Pharmaceuticals	70202	6
6.	Automobile Industry	57768	5
7.	Chemical except fertilizers	54735	5

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8.	Power	55356	5
9.	Metallurgical Industries	47834	5
10.	Hotel and Tourism	46656	4

The Administrations sector is bringing in the most money (27 percent of absolute FDI, or 298.882 crore), followed by Development and Improvement (27 percent offer, or 120.345 crore), according to the most recent data on FDI in India across various sectors. A sizeable portion of FDI is also going into other sectors of the Indian economy, such as communications, pharmaceuticals, PC software and hardware, the car sector, lodging, and travel.

According to the Economic Review of India, India's government sector grew at an annual growth rate of 9% from 2001 to 2012, making it the second largest in the world behind China at 10.9%. India ranks 10th in total GDP and 12th in total administrative GDP in 2012, and ranks 15th among the world's largest economies. India has the fastest growing government sector after China, with compound annual growth of 9% over the last 11 years from 2001 to 2012. This may be because the largest share of FDI was invested in this sector.

6.3. FDI and India's GDP

The most important factors affecting every nation's economy are foreign direct investment and total national output. FDI directly affects a country's GDP, therefore there is no doubt that the two are connected. There are innumerable quantitative and subjective economic and non-economic elements that have an impact on a country's gross domestic product; FDI isn't the primary economic component that determines whether it increases or decreases.

Table 3: For the aforementioned data, the 2000–2010 period's Karl Pearson's coefficient of correlation

Year	GDP-Real growth rate (%)	Equity inflows in Million (US$)
2000-2001	6.6	3807
2001-2002	7	5333
2002-2003	5.2	4245
2003-2004	5.2	3667

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2004-2005	7.2	3458
2005-2006	5.3	4435
2006-2007	7.3	5072
2007-2008	8.3	8366
2008-2009	8	27807
2009-2010	9.3	26703

A quantified study reveals a close link between gross domestic product growth and value flows to India via GDP. As a result, the rate of GDP growth increases with each increase in FDI input. The two variables are not perfectly correlated, as can be seen, and the Gross Domestic Product Growth Rate is fluctuating excessively. We can infer from this that they are somewhat positively connected to one another. Additionally, we might say that there are just too many diverse factors that influence India's GDP. Other factors could be the cost of the loan, the rate of work, the rate of expansion, and so forth.

7. Findings

1. The growth of FDI in India shows a positive trend and is a very reliable indicator of the Indian economy.

2. Indian economy is one of the major barriers to investment for most developed and developing countries.

3. There is a positive correlation between the FDI and FII inflows to India.

4. Since FDI and Indian GDP have a positive correlation coefficient of 0.6, FDI as a whole is helping to India's economic growth.

5. Over the last 11 years from 2001 to 2012, India's services sector registered an annual growth rate of 9%, only 9% lower than China's 10.9%. For this reason, the Indian services sector receives the majority of foreign direct investment in India.

8. Conclusion

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Both the host nation and the foreign financial supporter can gain most from foreign investments in terms of financial and social commitments. The lack of a solid basis and psychological oppression problems are the biggest barriers to progress in this strategy. Those countries that have found solutions to these problems are greatly benefiting from international investments. The pattern of foreign direct investment into the Indian economy is growing rapidly and vertically. According to the above study, the Indian economy is one of the most attractive investment barriers for the majority of developed and agricultural countries. Additionally, we should change the guidelines and rules governing FDI in India in order to throw open this door. But even if India experienced a sizable FDI infusion just after the recession, I can't help but wonder. why it's difficult for us to draw in more FDI. Given that India's FDI growth rate from 2010 to 2014 was not very favourable. We therefore aim to identify a few variables that are preventing FDI inflow into the Indian economy.

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