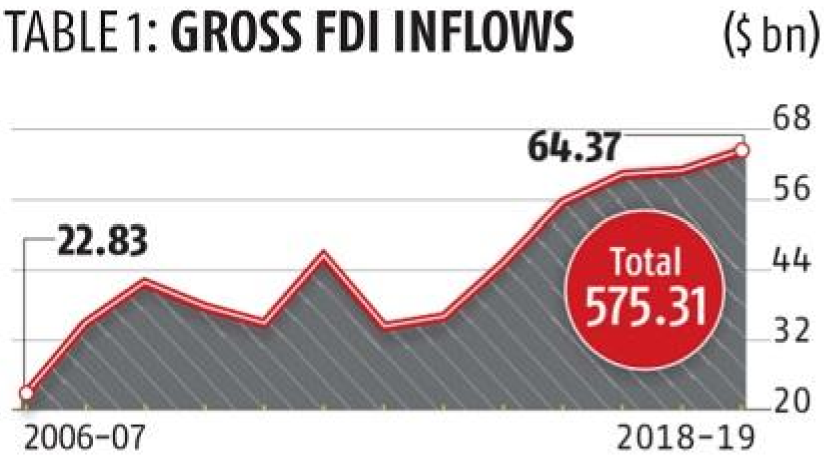
$5 Trillion Economy by 2024 - Significance of FDI

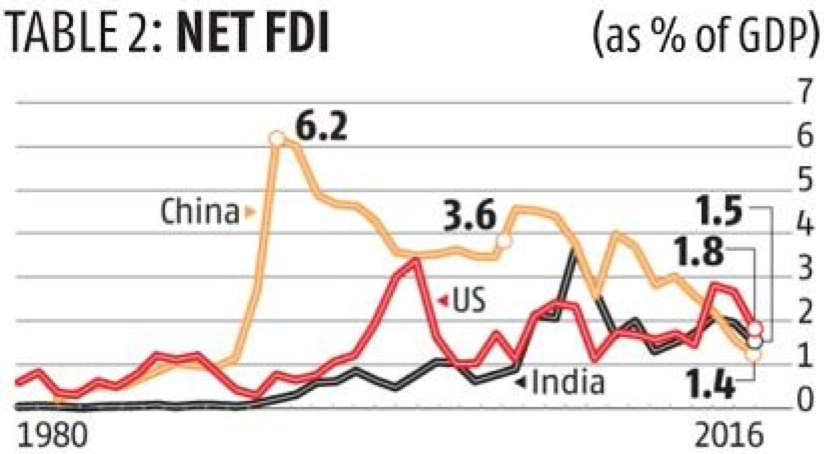
What is the issue?

- PM, in the NITI Aayog's 5th Governing Council meeting held recently, called for making India a $5 trillion economy by 2024.
- Here is an assessment of Foreign Direct Investment (FDI) status in India, in this regard.

What is the current FDI scenario?

- **Gross inflows** of foreign direct investment (FDI) rose to $64.37 billion in 2018-19.
- [It was stagnated at around $60 billion for the previous two years.]
- The gross FDI inflows have nearly trebled since 2006-07 when it was mere $22.8 billion.
- Evidently, despite domestic economic ups and downs, foreign investors have retained faith in the Indian economy.
- **Net FDI inflows** – It is the net FDI inflows that actually contribute towards balancing the country's external account and boosting economic activity.
- Encouragingly, net FDI inflows in 2018-19 increased to around $45 billion from around $39 billion in 2017-18.
- This represents a much needed acceleration in these flows with growth rate in FY19 touching 15%.
- This is in sharp contrast to the previous two years, when net FDI inflows had actually declined by (-) 6% and 6.6% respectively.
- Thus, net flows in 2018-19 have staged a comeback and marginally surpassed the peak of $44.9 billion reached in 2015-16.





What do other indicators show?

- **Recipient of FDI flows** - According to UNCTAD (World Investment Report), India is now the 10th largest recipient of FDI flows.
- [The US leads the list with attracting $252 billion through FDI in 2018.]
- **Cross-border investment flows** - India's share in global cross-border investment flows has increased from 2% in 2010 to 3.2% in 2018.
- **Share in GDP** - World Bank data (World Development Indicators) shows that the share of net FDI inflows in India's GDP has less than halved over the years.
- It had peaked in 1999 at 3.6% of GDP and has since then declined to stand at 1.6% in 2017.
- Having staged a comeback in 2018-19, the share would be slightly higher now.

How does India compare with China?

- In terms of share in GDP, India's FDI performance looks comparable in 2017 to both China and the US.
- However, now, with its GDP nearly 5 times the size of India's economy, China managed to attract $129 billion in 2018.

- Also, since its structural reforms in 1982, China has seen remarkable economic performance driven by a persistent pursuit of FDI.
- Consequently, the share of net FDI inflows in Chinese GDP rose from about 0.2% in 1982 to 6.2% in 1993.
- During this time, per capita incomes in China also rose from $203 to $377 and have maintained this rising trajectory.
- India's net FDI inflows as a percentage of GDP has been negligible in 1982, but increased and peaked in 2008.
- But even at its peak, FDI's share in India's GDP was just more than half of Chinese peak levels.
- Also, in 1991, per capita incomes in China and India were at somewhat similar levels (6-7%) of global average per capita incomes.
- By 2018, Chinese per capita incomes were more than 85% of global averages.
- On the other hand, India's per capita incomes just reached up to 18% of the global averages over this period.
- **Reason** - India decided to reduce the dependence on foreign investors for creating additional jobs and spurring economic growth.
- It decided this at a much earlier stage compared to China.
- This is one of the reasons for the low FDI levels in India.

What is to be done?

- India has always had a thriving entrepreneurial community with access to domestic investible pool, generated principally by domestic household savings.
- FDI finances hardly account for 5% of the country's total investment.
- Clearly, FDI inflows need to be given a special treatment over that extended to domestic investors.
- India has to now discuss the relative merits and demerits of pursuing a policy that seeks to attract greenfield FDI inflows.
- [Greenfield inflows - create new capacity and employment; brownfield inflows - go towards acquisition of existing assets.]
- In this process, there is also the need to distinguish between "tariff jumping" versus "export oriented" FDI.
- [Tariff-jumping FDI allows a foreign firm to avoid a trade barrier by locating production within the destination market.]
- As widely acknowledged, the export-oriented FDI (manufacturing within) is seen to have more positive economy wide impact.
- In all, a clear and consistent position has to be evolved as regards with the FDI policy, which addresses the priorities of all stakeholders.
- This will ensure that there is greater predictability at all levels towards FDI.

- In India’s efforts to take the economy to $5 trillion, such clarity, and a unified and predictable policy is a much needed one.

Source: Business Standard