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Impact of Foreign Direct Investment, Imports and Exports

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Abstract

This study sought to elucidate the existence of a link between Foreign Direct Investment (FDI) Exports and Imports in India. In addition, this study uncovered the importance of other determinants of Exports and Imports performance. The impact of FDI inflows on the export and import performance of india. The liberalization policy automatically helped increase the FDI inflow into India. This study make an attempt to analyze the impact of FDI on the import and export performance in India.

Keywords: *Foreign Direct Investment, Economic Development, Exports and Imports.*

1. Introduction

Foreign Direct Investment (FDI) is a potent instrument of economic development, especially for the less developed countries. It enables capital-poor countries, like India, to build up physical capital, create employment opportunities, develop productive capacity, enhance skills of local labour through transfer of technology and managerial know-how, and help integrate the domestic economy with the global economy. In integrating the local economy with the global economy, it affects the Balance of Payment (BoP) of country.

Foreign Investments provide a great impetus for growth to Indian economy. The continuous upsurge in foreign direct investments (FDI), allowed across the industries and sectors, has proven that foreign investors have faith in the resilience of Indian markets. A wise policy regime and positive business environment have also played catalytic role to ensure the continuous inflow of foreign capital in the Indian markets. Various surveys and industry experts have revealed that India is amongst the top destinations for investments across the globe. Certain facts and figures, pertaining to latest FDI developments, have been discussed hereafter.

2. Foreign Direct Investment

Foreign Direct Investment (FDI) plays an extraordinary and growing role in global business. It can provide a firm with New Markets and Marketing Channels, Cheaper Production Facilities, Access to New Technology, Products, Skills and Financing. For a host country or the foreign firm which receives the investment, it can provide a source of New Technologies, Capital, Products, Organizational Techniques, Management Skills, and as such can provide a strong impetus to Economic Development**.** FDI is a measure of foreign ownership of domestic productive assets such as Factories, Land and Organizations. Foreign Direct Investments have become the major economic driver of globalization, accounting for over head of all cross-border investments.

2.1 Types of FDI

The types of Foreign Direct Investment are,

Green Field Investment is new facilities or the expansion of existing facilities. Greenfield investments are the primary target of a host nation's promotional efforts because they create new production capacity and jobs, transfer technology and know-how, and can lead to linkages to the global marketplace. However, it often does this by crowding out local industry; multinationals are able to produce goods more cheaply (because of advanced technology and efficient processes) and uses up resources (labor, intermediate goods, etc).

Mergers and Acquisition occurs when a transfer of existing assets from local firms to foreign firms takes place; this is the primary type of FDI. Cross-border mergers occur when the assets and operation of firms from different countries are combined to establish a new legal entity.

Cross - Border Acquisitions occur when the control of assets and operations is transferred from a local to a foreign company, with the local company becoming an affiliate of the foreign company. Unlike green field investment, acquisitions provide no long term benefits to the local economy-- even in most deals the owners of the local firm are paid in stock from the acquiring firm, meaning that the money from the sale could never reach the local economy.

Horizontal Foreign Direct Investment is investment in the same industry abroad as a firm operates in at home.

Vertical Foreign Direct Investment

Takes two forms

Backward Vertical FDI: where an industry abroad provides inputs for a firm's domestic production process

Forward Vertical FDI: in which an industry abroad sells the outputs of a firm's domestic production processes.

2.2 Definition of Import

A goods or services brought into one country from another country. Along with exports, imports form the backbone of international trade.

The higher the value of imports entering a country, compared to the value of exports, the more negative that country's balance of trade becomes.

The word import is derived from the word port, since goods are often shipped via boat to foreign countries. Countries are most likely to import goods that domestic industries cannot produce as efficiently or cheaply, but may also import raw materials or commodities that are not available within its borders.

2.3 Types of Import

Industrial and Consumer Goods

Intermediate Goods and Services

2.4 Definition of Export

A function of international trade whereby goods produced in one country are shipped to another country for future sale or trade. The sale of such goods adds to the producing nation's gross output. If used for trade, exports are exchanged for other products or services.

Exports are one of the oldest forms of economic transfer, and occur on a large scale between nations that have fewer restrictions on trade, such as tariffs or subsidies.

Most of the largest companies operating in advanced economies will derive a substantial portion of their annual revenues from exports to other countries. The ability to export goods helps an economy to grow by selling more overall goods and services.

One of the core functions of diplomacy and foreign policy within governments is to foster economic trade in ways that benefit both parties involved.

2.5 World Exports, Imports and FDI Inflows

	Years		
	1990-1994	**1994-1999**	**2000-2005**
Exports	37,20,338	53,94,946	76,56,527
Imports	38,32,498	54,94,774	79,40,450
FDI Inflows	2,01,002	6,06,884	8,40,742

(Sources: www.Tradingeconomics.com)

2.6 Export and FDI

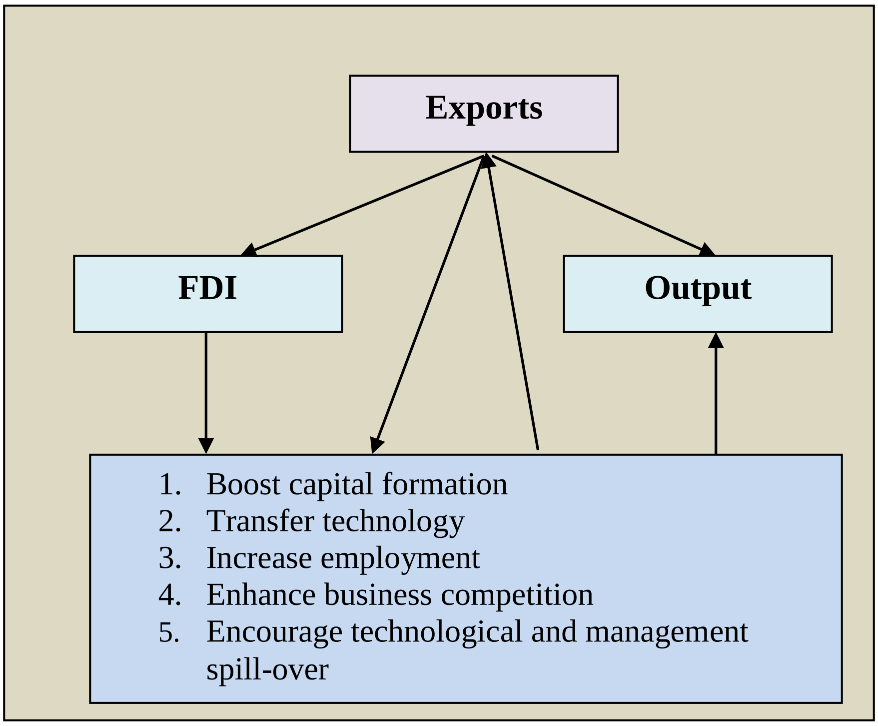
FDI and international trade are not only increasingly complementary and mutually supportive, but also increasingly inseparable as two sides of the process of economic globalization (Ruggiero 1996). Furthermore, inward FDI may stimulate exports from domestic sectors through industrial linkage or spill-over effects, Harrison, 1993). This effect creates a strong demand stimulus for domestic enterprises and promotes exports. FDI is expected to affect export from the export supply side of the host country. FDI may enhance export-oriented productivity that further improves export performance. Others may argue that export leads to increase in productivity that further attracts foreign investors to undertake FDIs.

Export contributes to growth by facilitating labour mobilization and capital accumulation. In theory, there is a two-way causal relationship between trade and productivity, although advocates of export-led growth generally contend that exports enhance productivity growth. These economists argue that firms tend to learn advanced technologies through exports and must adopt them to compete in the foreign marketplace. Firms also learn by doing, and emulate foreign rivals through trial and error inherent in the production and sale of export goods.

Furthermore, the expansion in production resulting from exports reduces unit production prices, thus increasing productivity. In addition to these effects, exports also provide a country with foreign exchange, which is often scarce in the early stages of economic development, enabling a country to import capital and intermediate goods.

Thus, for a variety of reasons, exports increase productivity growth. The reverse causation from productivity growth to exports is also intuitively straightforward. Productivity growth improves a country’s international competitiveness in price and quality, and thereby boosts its exports.

2.7 Possible links in FDI and Exports



2.8 Import and FDI

Studies on the effect of FDI on import are scant. FDI both at the initial investment and operation phases can influence import of a country. At the initial investment phase, import of equipments, machineries, installation facilities and experts all contribute to increased import balance. FDI companies have high propensities to import capital and intermediate goods and services that are not readily available in the host country.

In the later phases of the investment; input nature, output type, productivity spill-over and type of relationship with other role players in the industry determine the direction of effect of FDI on import of a country. If FDI uses local raw materials and other inputs of production, it may not have significant adverse effect on import.

On the contrary, if it relies on imported inputs like raw material, human skill, and other intangibles assets, it affects import positively. The relationship between import and output type of FDI can be positive or negative.

If the output is complementary to other products that are imported, it may encourage import and would have positive effect. However, if FDI is concentrated in import substituting industries, then it is expected to affect imports negatively because the goods that were imported earlier would now be produced in the host country by foreign investors.

The effect of productivity of FDI and spill-over from FDI on import can be seen together. The theoretical relationship between imports and productivity, and hence FDI, is more complicated than that of exports and productivity. Increased imports of consumer products encourage domestic import-substituting firms to innovate and restructure themselves in order to compete with foreign rivals; therefore, imports enhance productive efficiency.

It can also attract foreign firms to undertake investment activities to supply the market. These MNEs, with their experience in supplying both the foreign market and the potential host countries' market previously, are better suited to mobilize factors of production to the host country and engage in production. If that is the case, imports would be discouraged because of domestic supply from MNEs' production facilities. By the same logic, with the positive technological, human capital and other spill-over from foreign firms to local firms, domestic firms could contribute further to the import substitution effect leading to decreased import.

Another channel of FDI effect is dependent on the kind of relationship with different levels of the value chain in the industry. In a forward integration, an FDI may be engaged in further processing of a partially processed output of a local company that used to be exported for further processing in a foreign company. This production process may render the product extra quality that makes it usable at the local market. That would have a negative effect on import and export. In a backward integration, an FDI may undertake production of an item, which is an input for another production facility.

If that intermediate product was an import item, such kind of integration would have a negative effect on import. With all these possible directions of outcomes, FDI may have positive or negative effect on trade balance.

2.9 Calculation of FDI, Imports and Exports Growth Rates

Months / Factors	FDI (USD Million)	% of Inc/Dec	Imports (INR Billion)	% of Inc/Dec	Exports (INR Billion)	% of Inc/Dec
January	871		2209.13		1302.94	
February	484	-44.43	1963.63	-11.11	1238.74	-4.93
March	219	-54.75	2129.92	8.47	1451.23	17.15
April	1542	604.11	1958.9	-8.03	1231.37	-15.15
May	1133	-26.52	2218.14	13.23	1349.84	9.62
June	1220	7.68	2004.53	-9.63	1396.45	3.45
July	1570	28.69	2250.80	12.29	1284.17	-8.04
August	3010	91.72	2078.59	-7.65	1215.40	-5.36

September	4111	36.58	2282.61	9.82	1302.14	7.14
October	685	-83.34	2377.59	4.16	1215.63	-6.64
November	1424	107.88	2277.96	-4.19	1192.73	-1.88
December	1285	-9.76	2325.24	2.08	1339.14	12.28
Total	**17554**		**26077.04**		**15519.78**	
Mean	**1462.83**		**2173.09**		**1293.31**	

(Sources: www.Tradingeconomics.com)

The above table shows that the Exports, Imports and FDI inflows during the year of 2012. The maximum of 4111 USD Million Foreign Direct Investment inflows receives during the month September. Further the Growth Rate of FDI shows positive growth was observed only during the months April, June, July, August, September and November.

Majority of Rs.2377.59 Billion imports in the month of October 2012. Further the Growth Rate shows positive growth was observed only during the months of March, May, July, September, October and December. The maximum of Rs.1451.23 Billion experts during the month of March 2012. The Growth Rate shows positive growth was observed only during the months of March, May, June, September and December.

The total of Foreign Direct Investment, Imports and Exports shows that 17554, 26077.04 and 15519.78 respectively. The Mean of Foreign Direct Investment, Imports and Exports shows that 1462.83, 2173.09 and 1293.31 respectively.

3. Conclusion

The present study, as against a number of previous studies, has provided adequate and statistically significant evidence of positive linkage between FDI and exports, Import. The FDI could not be assumed as the only explanatory variable for predicting variations in exports. International trade that is measured either by exports or by imports is found to be complementary to FDI inflows. FDI inflows are observed to have feedback effects with exports of the trading partners and of the other trading partners. Similar linkages between FDI inflows to, and imports by, the trading partners and the other trading partners are also revealed. FDI induced by trade expansion will also improve social welfare. It is important for both the public and private sectors to realize the complementarily between trade and investment, and respond accordingly.

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