Foreign Direct Investment (FDI)

6.50 Aggregate FDI inflows declined by more than US$ 1 billion in 2002-03 to US$ 3.6 billion from US$ 4.7 billion in 2001-02. Net FDI inflows are sum total of FDI inflows into India and FDI outflows from India. A category-wise analysis reveals that net FDI inflows into India were lower by US$1.5 billion in 2002-03, compared with 2001-02 (Table 6.2). According to the revised system of data reporting for FDI inflows adopted recently by the RBI in line with the international best practices (Box 6.4), FDI inflows comprise equity inflows, reinvested earnings and other capital. The overall decline in 2002-03 was principally on account of a sharp drop in net equity inflows. The analysis points to a slackening of fresh equity injected through FDI in the year 2002-03, which might be indicative of a commensurate decline in new investment projects. FDI outflows from India, which reflect the long term investment commitments of Indian multinationals in foreign markets, showed a decline of US$ 0.34 billion in 2002-03, reflecting lower interests on part of Indian companies in direct investment abroad.

6.51 Net FDI inflows maintained their subdued trend in the first nine months of 2003-04, registering a marginal decline of US$ 0.25 billion compared to the corresponding period of the previous year. Equity FDI inflows into India recorded a lower volume of US$ 3.2

Box 6.4 : Revised FDI definition

A Committee was constituted by the DIPP in May, 2002 to bring the reporting system of FDI data in India into alignment with international best practices. Accordingly, the RBI has recently revised data on FDI flows from the year 2000-01 onward by adopting a new definition of FDI. The revised definition includes three categories of capital flows under FDI: equity capital, reinvested earnings and other direct capital. Previously, the data on FDI reported in the balance of payments statistics used to include only equity capital.

Conceptually, the main difference between FDI and portfolio investment is in the **lasting interest** expressed by a non-resident direct investor in a resident enterprise of the domestic economy. The **lasting interest** underlines a firm desire on part of the non-resident investor to be associated with the long-term business activities of the resident enterprise by exerting significant influence on the management of the enterprise. Accordingly, the international best practice systems have focused on recording of FDI data in balance of payments statistics in terms of three main categories as mentioned below:

1. equity flows (equity in branches, shares in subsidiaries and other capital contributions),
2. reinvested earnings (retained earnings of foreign subsidiaries and affiliates), and
3. inter-company debt transactions (inter-corporate debt transactions between associated corporate entities).

There are, however, considerable variations among countries as far as their reporting systems of FDI flows are concerned. China and India are good examples in this regard. The Chinese system of reporting FDI is much more broad-based. Apart from equity capital, reinvested earnings, inter-corporate debt transactions, China includes short-term and long-term loans, trade credits, bonds, grants, financial leasing, investment by foreign venture capital funds, earnings of indirectly held enterprises, non-cash equity acquisition, control premium and non-competition fee within FDI. It also includes project imports as FDI flows, which, in India, are recorded as imports. As compared to China, it is clear that till some time back, the reporting of FDI in India's balance of payments statistics, which was confined only to equity capital, represented a much narrower coverage of FDI flows.

It is interesting to note that adoption of a broader coverage system for FDI flows has resulted in upward revision of annual FDI inflows into India for the years 2000-01 and 2001-02 by US$1.7 billion and US$2.2 billion respectively, representing on average, a 70 per cent increase over previously reported data. While this is not to suggest that the difference between volume of FDI inflows into China and India is attributable only to the disparities in coverage of data, comparisons between the two nations in terms of their abilities to attract FDI, should take note of this point.

billion in April-December 2003, compared with US$ 3.6 billion in April-December 2002. FDI outflows from India were also recorded at a reduced level during April-December 2003-04. According to the data on monthly inflows of foreign investment compiled by the RBI, FDI inflows for the full year of 2003-04 have been estimated at US$ 4.5 billion, which are slightly lower than US$ 4.7 billion recorded during 2002-03.