The Most Alluring Future Destination For Foreign Direct Investments: A Case Study Of India.

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Abstract

Nearly two decades of economic liberalization, coupled with robust domestic demand, an emerging middle class, a young population, a high return on investment, cost competitiveness and an epic pool of talent endures to transform India as one of the most preferred destinations for FDI. India’s domestic demand-driven growth model is playing a catalyst role in enticing FDIs in the country. India is now transitioning into the next phase of the growth cycle where manufacturing might play a leading role in determining its growth trajectory. During 2007-11, India’s Top Five FDI Destinations (i.e. Bangalore, New Delhi, Pune, Mumbai and Chennai) enticed 1826 FDI projects creating above 378,548 jobs. We have enough evidence to comprehend that India is the next most alluring destination for FDIs. Hence, it is evident that India is the future Destination for FDIs.

Keywords: India, Foreign Direct Investment (FDI), Domestic Demand-Driven Growth, India’s Top Five FDI Destinations, Information Technology (IT), Case Study of India.

1. Introduction:

“Today India is changing and is becoming the land of opportunities. The pace at which India is growing, I can say with confidence that it will remain so for decades to come. India remains one of the top three investment destinations even in recessionary conditions and we are determined to maintain that position.”

—Anand Sharma, Minister for Commerce and Industry. (Doing Business in India, 2010)

With a population of more than 1.2 billion, India is the world’s largest democracy. Over the past decades, the economy has expanded in an impressive way. India has now emerged as a global player with the world’s fourth-largest economy in terms of purchasing power parity. (The World Bank: India Overview, 2012).

According to the International Monetary Fund (IMF) and CIA World Fact Book India is the 11th largest economy as per the nominal GDP for the year 2011 with a GDP of USD ($) 1.68 Trillion. Whereas, the United Nations and World Bank Accept India as the 9th largest Economy by GDP for the year 2011 with a GDP of USD ($) 1.72 Trillion and USD ($) 1.86 Trillion respectively (List of countries by GDP (nominal), 2012) (World Bank, 2012). India had a GDP growth rate of 6.8% for the year 2011 according to the World Bank and 7.2% according to CIA Factbook. India’s Merchandise Trade was 40% of its GDB in 2011 (World Bank: India, 2012). India has a Purchasing Power Parity of USD ($) 4.515 trillion in 2011 the 4th largest in the world (CIA Factbook India, 2012).

India is also undergoing a massive urban transformation. By 2030, the urban areas will be home to 40% of the country’s people — doubling the urban population within a span of thirty years. How India manages this urbanization will largely determine the long-term sustainability of its towns and cities, and quality of life for a sizeable part of its population (The World Bank: India Overview, 2012).

Did you know that India...

- is the world’s 2nd largest small car market and has the world’s 2nd largest pharmaceutical industry.
- is one of only three countries that makes its own supercomputers
- is the fourth largest economy in the world (measured in terms of purchasing power parity)
- is one of six countries that launches its own satellites
- 100 of the Fortune 500 have R & D facilities in India
- has the second largest group of software developers after the U.S.
- lists 6,600 companies on the Bombay Stock Exchange; only the NYSE has more
- is the world’s largest producer of milk, and second largest producer of food (fruits and vegetables)
2. Literature Review

"India is, the cradle of the human race, the birthplace of human speech, the mother of history, the grandmother of legend, and the great grand mother of tradition. Our most valuable and most instructive materials in the history of man are treasured up in India only."

- Mark Twain – American Author (1897)

2.1. Indian Economy:
With a gigantic population base the Indian economy is one of the world’s fastest growing economies (Harjeet, 2010). World Bank Accepts India as the 9th largest Economy by GDP for the year 2011 with a GDP of USD 1.86 Trillion (List of countries by GDP (nominal), 2012) (World Bank, 2012). India had a GDP growth rate of 6.8% for the year 2011 according to the World Bank and 7.2% according to CIA Factbook. India’s Merchandise Traded was 40% of its GDP in 2011 (World Bank: India, 2012). India has a Purchasing Power Parity of $ 4.515 trillion in 2011 the 4th largest in the world (CIA Factbook India, 2012). Even in rough times as of the financial meltdown the Indian economy presents the best investment opportunities. The latest trend followed throughout the developed world is investing in India or to do business on India soil. The Indian economy showcases its investment opportunities on the road to boost the foreign players to investing in India, to harness the excellent investment opportunities of doing business in India (Harjeet, 2010).

India is prominent as a great investment opportunity destination by developed countries due to the factors like cost effectiveness, ambitious economic reforms, reasonably better labour intensive Indian economy with good skilled, managerial and technical manpower and superior manufacturing conditions for investing in India. India has an abundant and diverse population to produce and consume goods. As the economic pace is picking up for India, the demand of a variety of products and services is escalating the investment opportunities for business in India. Performance of the Indian economy has been very well in last few years with augmented exports and good capital inflow to do business in India (Harjeet, 2010).

India has emerged as the 5th largest economy in the world and holds the 3rd largest GDP in the entire Asian continent. India offers high projection for investment prospect, business growth and return impending of the investments. Indian economy is seen as the potential market for future investment opportunity destination to do business by many of the world's popular brands. Indian economy is witnessing an increase in the FII investment by many folds. The economy of India is a world-class infrastructure and services which will definitely help to attract investment and business in India (Harjeet, 2010).

2.2. PESTEL Analysis of India:
We can analyze various different factors in a firm's macro environment by the use of the PESTEL framework. If a factor can emerges in numerous categories managers plainly make a decision of where they think it best belongs. This analysis helps managers decide whether the political, economic, social, technical, environmental and legal conditions are perfect in a country where they are going to invest. It is one of the most important analyses for investing in another country.

2.2.1. Political Factors:
Indian capital market is very fragile. In the past India has faced Political instability recently it has gained political stability. The capital market has witnessed a strong influence of the Political instability. Political changes affect India's share market significantly. BSE, SENSEX index rise and fall with any new policy of large and small. Indian capital market is feeble and speculation based. For developing the capital market of India, political stability in the country is crucial. The political factors consist of employment laws, tax policy, trade restrictions & tariffs and political stability (PESTEL analysis of Indian capital market, 2010).

The current political stability is a good indicator for attracting foreign direct investment. The performance of the political environment has been quite good in recent years. The current political situation in India is quite the exception to the relative strength of the ruling coalition. Under the leadership of the ruling Congress-led governing coalition, re-elected in May 2009, experiences rarely any challenges and is unite on the majority of issues that seem reasonable. This state of affairs in India is relatively scarce, but it lets the government continues to push the reform agenda, albeit in a wise manner (India, 2010).

2.2.1.1. Investment Environment:
Although India’s foreign investment policy allowed 100% foreign direct investment in most industries, but it does not arrive in India as a destination for direct investment. Government attempts to increase the flow of foreign direct investment from a number of obstacles, including rampant corruption, a bloated bureaucracy, and the failure of critical infrastructure constraints. India is famous for the variety of changing operational requirements and environment from one state to another. In February 2009, the government began changes to open, such as insurance, telecommunications, retail and other industries to foreign direct investment. Observers expect the government to adopt more economic reforms and investments, many of which provide opportunities for foreign investors (India, 2010).
2.2.1.2. Rates of Corporate Tax:

“Domestic corporations are subject to tax at a basic tax rate of 30%, as well as 10% surcharge. Foreign companies are subject to a basic tax rate of 40%, as well as a 2.5% surcharge... The effective tax rate for domestic corporations is 33.99% and for foreign companies 42.23%.”

(Doing Business in India, 2010)

2.2.2. Economical Factors:

The Indian government’s economic measures strongly relate to the capital market. The capital market fluctuates with the announcement of the annual budget and the economic policies of the government. The capital market takes it positively if the policies are encouraging to the companies but the capital market goes down if there are any other policies that are not accommodating, they are not welcomed (PESTEL analysis of Indian capital market, 2010).

As the allocation of 3 - G spectrum, those companies witnessed sharp growth in their share values who received the license for 3-G. Thus economic policies play an important role in the development and decline of financial markets. The economic factors incorporate inflation rate, economic growth, exchange rates and interest rates (PESTEL analysis of Indian capital market, 2010).

“Economic growth surged to 11.2% y/y in Q1 from an upwardly revised 7.3% in Q4, bringing the FY2009-2010 growth rate to 7.4%.”

(India, 2010)

2.2.2.1. Recent Performance:

Real GDP growth rose to 8.8% y/y in Q2-10, above the already strong 8.6% growth rate in Q1. On a seasonally adjusted basis however, real GDP slowed to 8.9% at an annualized rate from 13.5% in Q1. Almost half the y/y growth in Q2 came from personal consumption, which strengthened for the first time in 3 quarters despite tighter monetary policy, as more favourable weather has boosted farmers’ income, and public and private investment, heavily supported by infrastructure spending. Stronger imports constrained the overall growth figure, but at the same time reflect healthy domestic demand (India, 2010).

2.2.2.2. Fiscal Policy:

The budget for the 2010-11 fiscal year marks the beginning of consolidation efforts after the stimulus measures and the fiscal slippage of the previous two years due to elections and large one-time spendings. As a share of GDP, the deficit is expected to reach 7.8% of GDP (including off-budget food, fuel and fertilizer price subsidies of 1.7% of GDP) from 9.6% 2009-10 and 11.8% in 2008-09. The improvement will come from reduced subsidies and greater revenues from the acceleration of economic growth, as well as the one-time sale of G3 licenses, which generated over USD 15 billion (India, 2010).

2.2.2.3. Monetary Policy:

With waning inflationary pressures and weakening industrial activity, the Reserve Bank of India (RBI, the central bank) may ease on its tightening cycle. Reserve requirements and the main interest rates have been raised by 125 basis points for the repo rate and 175 basis points for the reverse repo, since the beginning of the year. However, M2 growth remains unusually strong and the impact of the Pakistani floods and the Russian grain export ban may renew inflationary pressures. For now however, the Wholesale Price Index (WPI), the RBI’s target indicator for inflation, eased to 8.5% in August, slowing for the fifth consecutive month since peaking at 11% in April (India, 2010).

2.2.3. External sector:

Strong investor appetite for Indian bonds and equities are driving capital inflows in the country, boosting the currency at the same time. The stronger currency has exacerbated pressure on the trade sector, as healthy domestic demand and weakening export growth are driving up the trade and current account deficits, despite strong transfers from abroad, and the return of external demand for India’s software services (India, 2010).

2.2.4. Social Factors:

India is a country of unity in diversity. Despite the social richness of India the capital market is not very much linked to the social factors. Although capital market has some relation with the social factors but the big social factors have a minute effect on the capital market where as small social factors don’t impact at all (Harjeet, 2010). McDonalds was forced by the social environment to offer vegetable burger and vegetarian food in India instead of beef and chicken. But the overall impact of such social issues is minimal on business. Like McDonalds is now working successfully in India.

The large population base of India provides for a huge market for many types of products. Thus one would not have to worry about market demand due to the large and diverse population with an excess of the working class and medium income group. Consumer goods production and sale is one of the most profitable and least risky businesses in India. This huge pool of people also provides an abundance of people finding work. This gives investors an advantage to exploit the cheap labour – skilled or unskilled.
2.2.4.1. Languages:
English enjoys the status of subsidiary official language but is the most important language for national, political, and commercial communication. As a good number of Indians can speak and write English thus giving India a huge advantage over China which is struggling to teach English to its people who never before felt the need to study English. Hindi is the most widely spoken language and primary tongue of 41% of the people; there are 14 other official languages (CIA Factbook India, 2012).

2.2.4.2. Labor force:
487.6 million (2011 est.) which has been ranked the 2nd largest in the world. As per 2009 estimates 52% of the Indian labour force works in the agriculture sector, 14% in the industrial sector and 34% in the services sector. In 2011 India had an unemployment rate of 9.8%, whereas 25% of Indians live below the poverty line in 2007 (CIA Factbook India, 2012).

“Despite some outstanding examples of individual achievement of Indian women and a definite improvement in their general condition over the last century, it remains true that Indian women still constitute a large body of under-privileged citizens... balancing work and family is a major hurdle for working women. While family responsibilities influence the careers of all parents, women (particularly those with newborns and preschoolers) may have disproportionate work in care of children/home. Being a woman itself poses various problems to an individual. The problems of Indian women pertain to her responsibility towards family, society and lion work.” (Shafique et al., 2012)

Despite shedding light on these facts (Shafique et al., 2012) concludes that the traditional trends are changing and women are now encouraged to work and are supported by their parents and husbands in this regard. Although this research is based in Pakistan but it can be generalized to India as the cultural differences between the two countries are not much different and the countries themselves share a large border therefore they are not separated geographically as well. Therefore it can be concluded that the female workforce of India is now encouraged to playing a vital part in the development of their country.

2.2.5. Technological Factors:
The Indian capital market is nominally affected by technological factors. India is technological backward country. Technological factor can affect on an individual company but it has no a large impact on the entire capital market, same as the case with social factors. India experiences technological change mostly on a lower basis and thus it never affects on the whole country. The technological factors embrace R&D activity, technology incentives, rate of technological change and automation (Harjeet, 2010).

India is now rapidly developing and adapting to new technologies and is fast becoming another technologically advanced country. India is investing rapidly in research and development. Although technological factors don’t play a vital part in the capital market of India and that is because India is a labour intensive country. But India is moving towards technologically advanced and capital intensive country. Bangalore has now become the silicon valley of India.

2.2.6. Enviornmental Factors:
Primarily the environmental factors didn’t play a critical role in the capital market. But now the time has changed therefore people are becoming more eco-friendly. In India this are really concerned about this that either any firm or industry is environment friendly or not. An ever increasing number of people, investors and corporate executives are focusing on these facts while the capital markets still perceives the environment as a liability. They belive that it’s useless for their strategy. The environmental performance is even under-valued by the markets (Harjeet, 2010).

2.2.7. Legal Factors:
Legal factors play a pivotal role in developing and sustaining the Indian capital market. The fate of the capital market is determined by the Legal issues relating to any industry or firm. In case the Indian govt. or parliament introduces a new law that can affect the operation of the industry will result in the fall of capital market as the industry will be demotivated and this demonization will lead to the demonization of the investors (Harjeet, 2010).

2.3. Investment Opportunities in India:

The rudiments that make India attractive to investors remain intact as the inordinate potential of the domestic market driven by an emerging middle class, cost competitiveness and an epic pool of talent endures to transform India as one of the most preferred destinations for FDI. India’s domestic demand-driven growth model
is playing a catalyst role in enticing foreign investments in the country. India is now transitioning into the next phase of the growth cycle where manufacturing will, most probably, play a leading role in determining its growth trajectory. Despite the fact that India is a leader in the world ranking as a shared services destination, it is swiftly emerging as a manufacturing location for countless foreign corporations (Ernst & Young's: India attractiveness survey, 2012).

In 2011 India persisted to be a very alluring destination for FDI being the 4th most enticing target for FDI in terms of projects which augmented by 20% in the course of a year. This engrossed 932 projects creating around 255,416 jobs and all this in a global economic scenario that hadn’t entirely recovered from the 2008-09 financial crises and is slow again, from over 5% in 2010 down to a projected 3.3% through 2012 (Ernst & Young's: India attractiveness survey, 2012).

Investors arrive at India looking for growth opportunities in their business and to exploit the benefits of lower operating costs. (Ernst & Young's: India attractiveness survey, 2012) discovered that 55% of its panel assertions that India’s colossal and growing domestic market is their number one enticement, whereas 45% of them comprehend India as a highly cost-competitive location.

2.4. India’s Top Five FDI Destinations:
Top five Indian cities entice 42% of the investment projects, 36% of the jobs generated through FDI and 28% of the value of FDI (Ernst & Young's: India attractiveness survey, 2012). These cities are:

2.4.1. Bangalore
Bangalore is India’s version of the Silicon Valley. It’s now a global hub for service sector investment in IT, engineering and biotech as a result of Bangalore’s Millennium IT Policy and Millennium Biotech Policy, which presents a range of enticements to attract technology companies. During 2007-11 the city has successfully initiated 474 investment projects creating above 110,140 jobs through FDI based on its educated workforce and high-quality infrastructure (Ernst & Young's: India attractiveness survey, 2012).

2.4.2. New Delhi
New Delhi is a destination of interest for the services industry, for the most part IT and IT enabled Services (ITeS), and consultancy. The city has developed as a strategic location for the launch of foreign company branch offices. During 2007 and 2011 the city engrossed 305 FDI projects creating above 34,100 jobs (Ernst & Young's: India attractiveness survey, 2012).

2.4.3. Pune
Pune possesses a large industrial base attracting substantial foreign investments in the manufacturing sector. Apart from that Pune now adores to develop into a key hub of software and IT services. Throughout 2007 to 2011, the city engrossed 248 FDI projects creating above 70,700 jobs (Ernst & Young's: India attractiveness survey, 2012).

2.4.4. Mumbai
Mumbai being the commercial capital of India engrossed 461 FDI projects during 2007 to 2011, creating above 54,900 jobs. Mumbai attracts investors to exploit its manufacturing and services opportunities particularly targeting energy, transportation, software and banks / financial services institutions. The state government facilitates investment through its policies for biotech, e-governance, infrastructure, IT, special economic zones and tourism (Ernst & Young's: India attractiveness survey, 2012).

2.4.5. Chennai
Chennai is celebrated for its automotive sector, especially in automobile and railway coach manufacturing, design, development and testing. 338 investment projects were initiated in Chennai during 2007 to 2011 creating 108,708 jobs (Ernst & Young's: India attractiveness survey, 2012).

"It is already becoming clear that a chapter which had a Western beginning will have to have an Indian ending if it is not to end in the self-destruction of the human race. At this supremely dangerous moment in history, the only way of salvation for mankind is the Indian way."

- Dr Arnold Toynbee – British Historian.

3. Conclusion:
Nearly two decades of economic liberalization, coupled with robust domestic demand, a growing middle class, a young population and a high return on investment, make India a credible investment destination for any Investor. A growing India offers opportunity across sectors — notably infrastructure, pharmaceuticals, automobiles, education and many more — in an investor-friendly environment.

With its one billion plus population the Indian market offers profitable and assorted opportunities for foreign exporters with the right products, services, and commitment. As the Indian economy further globalizes and develops in the mid-term its requirements for equipments and services for major sectors such as energy, environmental, healthcare, high-tech, infrastructure, transportation, and defence will exceed tens of billions of dollars. With GDP growing at 6.8% to 7.2% (for 2011) India is one of the fastest growing economies in the
world and the second fastest in Asia. India can potentially sustain growth of 7-10% for a few more years.

Irrespective of the current crisis, a strong surge in the number of Foreign Direct Investment (FDI) projects in India proves that India is undoubtedly an attractive investment destination. A large number of people and researches are convinced regarding India’s enduring prospects. India is now transitioning into the next phase of the growth cycle where manufacturing will, most probably, play a leading role in determining its growth trajectory. Despite the fact that India is a leader in the world ranking as a shared services destination, it is swiftly emerging as a manufacturing location for countless foreign corporations. India is expected to be one of the world’s three leading destinations for manufacturing by the year 2020.

The rudiments that make India attractive to investors remain intact as the inordinate potential of the domestic market driven by an emerging middle class, cost competitiveness and an epic pool of talent endures to transform India as one of the most preferred destinations for FDI. India’s domestic demand-driven growth model is playing a catalyst role in enticing foreign investments in the country.

In the course of 2007 to 2011, India’s Top Five FDI Destinations enthralled 1826 FDI projects creating more than 378,548 jobs. All this in a global economic scenario that hadn’t entirely recovered from the 2008-09 financial crises and is slowing again, from over 5% in 2010 down to a projected 3.3% through 2012. Top five Indian cities entice 42% of the investment projects, 36% of the jobs generated through FDI and 28% of the value of FDI in India. These cities are Bangalore (India’s version of the Silicon Valley), New Delhi (India’s Capital), Pune (Industrial Hub), Mumbai (the commercial capital of India were dreams come true) and Chennai (celebrated for its automotive sector).

Unlike western societies, in India religion, fatalism and collectivism are all components of daily life and they need to be respected for a healthy and successful business relationship. Despite the traditional caste system being dismantled, remnants may still be witnessed in the Indian hierarchical structure of business practices and decision-making. There is a strong sense of tradition tied into daily business practices. Yet, signs of change are becoming more evident. Ever since the economic reforms began in 1991, India’s market is growing rapidly. There is enough evidence to suggest that India has now started to make use of its untapped women workforce which is favourable indicator of its progress towards becoming a hub for international businesses.

With its geographical positioning in the Indian Ocean, a major international trade route, and with its rich mineral and agricultural resources, India’s economy is witnessing increased inflows of foreign investments. India is also recognized for its competitive education system and vast pool of highly skilled labourers, making it an attractive market for foreign businesses.

To put it in a nutshell we can say that India provides a great opportunity for foreign direct investment and scores fairly well on the PESTEL Analysis. Investors arrive at India looking for growth opportunities in their business and to exploit the benefits of lower operating costs. India’s colossal and growing domestic market is the number one enticement for countless investors. Throughout our investigation we found India to be the most desirable choice for foreign direct investment in the years to come. India has all the necessary elements that lead a country and its business to succeed. We have enough evidence to comprehend that India is the next most alluring and enticing destination for foreign direct investments. Hence, it is evident that India is the future face of foreign direct investments.

"If there is one place on the face of this Earth where all the dreams of living men have found a home from the very earliest day when man began the dream of existence, it is India."

- Romain Rolland – French Philosopher (1929)

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