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Analysis of Foreign Direct Investment in Indian Food Processing Industry During Post Reforms

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ABSTRACT

A strong and dynamic food processing sector plays a considerable role in the overall economic growth of a country. The sector employed large numbers of people, many of whom are unskilled laborers. Since the establishment of the ministry of food processing industry in 1988, the food processing industries acknowledged close attention of this sector. Food sector has the large chain of industries producing inputs & commodities. For the growth of this sector, there is an ample need of capital, which can be fulfill from foreign direct investment (FDI) inflows. In developing economies, food processing industries play a vital role by generating employment and income opportunities. The sub sector generates backward employment linkages by creating markets for raw materials and forward employment linkages, as people engaged in the supply of processed food. Developing nations always like to attract direct investment from developed nation due to potential technology spillovers. Foreign direct investment is one of the key drivers of growth and usually regarded as valuable for the host countries in which FDI flows are intended for. This study focused on the trends and pattern of foreign direct investment in Indian food processing industry from the period 1991-2015.

Keywords: Foreign direct investment, Food processing industry, FDI Inflows.

INTRODUCTION:

A strong and dynamic food processing sector plays a considerable role in the overall economic growth of a country. Food processing is the conversion of raw material into food or of food into other forms, by physical or chemical means. It produces marketable food products that can be prepared instantly and liked by the consumers. The term 'food processing' is mainly defined as a process of value addition to the agricultural or horticultural produce by various methods like grading, sorting and packaging (MOFPI). Food processing is a process in which food is prepared for consumption. The sector employed large numbers of people, many of whom are unskilled laborers. Since the establishment of the ministry of food processing industry in 1988, the food processing industries acknowledged close attention of this sector. Food sector has the large chain of industries producing inputs & commodities. In developing economies, food processing industries play a vital role by generating employment and income opportunities. The sub sector generates backward employment linkages by creating markets for raw materials and forward employment linkages, as people engaged in the supply of processed food (Tisimia, 2014). Food processing industries include cannery, meat packing plant, fish processing, slaughterhouse, food packing plants and sugar industry etc. Foreign direct investment is one of the key drivers of globalization and usually regarded as the valuable for the host countries in which FDI flows are intended for. The investments in which foreign funds are injected in the enterprise of the other nation of origin from the investors are called as FDI. The rights of management and voting are granted to the investors if the level of ownership more than or equal to 10% of ordinary shares. In case of, less share of ownership than the stated amount is termed as foreign portfolio investment (FPI). So FDI is an investment in the form of controlling ownership in an enterprise in one nation by an entity based in another nation and it is thus distinguished from FPI by a conception of direct control. According to the Financial Times, "Standard definitions of control use the internationally agreed 10 percent threshold of voting shares, but this is a grey area as often a smaller block of shares will give control in widely held companies. Moreover, control of technology, management, even crucial inputs can confer de facto control." The foreign direct investors may acquire voting power of an enterprise by incorporating a wholly owned subsidiary, or through merger or acquisition, or by participating in an equity joint venture, or by buying shares in a related enterprise. Portfolio investment covers external claims in equity and debt securities, other than those included in direct investment and reserve assets. Debt instruments include long-term bonds and notes, short-term money market instruments, and financial derivatives such as options, warrants, traded financial futures, and currency (but not interest rate) swaps.[i] Global FDI fell by 13% in 2016 but modest recovery would be expected in 2017. Foreign direct investment (FDI) is defined as an investment involving a long-term relationship and reflecting a lasting interest in and control by a resident entity in one economy of an enterprise resident in a different economy (UNCTAD, WIR 2009). Since 1980, Foreign Direct Investment has become the most important determinant of economic growth of the host country. It also plays a vital role to improve the human capital, market, productive efficiency and technology of the host country and also create employment opportunities. FDI can be categorized into three parts viz. Horizontal FDI, Vertical FDI and Platform FDI. These three types of FDI's can be differentiated on the bases of activities. FDIs can also be classified as Inward FDI and Outward FDI. These can be differentiated on the basis of direction of flow of money. When a foreign entity either purchase or invest in the new or existing business in a nation different than the investing company's origin is called an inward investment or foreign direct investment. FDI help the entities to grow and open the borders for international integration. Methods of FDI include the opening of a subsidiary in foreign country, or acquiring control in the existing foreign company, or by the means of merger or joint venture with the foreign entity. Outward direct investment is the investment made by residents of reporting nation to the external economies. This is also called as direct investment abroad. So foreign direct investment is a cross border investment associated with the resident in one nation a significance degree of control on the management of a company that resides in another nation. Data on FDI flows are presented on net bases. Data on FDI net inflows and outflows are based on the sixth edition of the Balance of Payments Manual (2009) reported by the International Monetary Fund (IMF). At present time the issue of FDI is being paid more attention by the academicians and policy makers at national and international level. Several empirical studies on the relationship between FDI and Economic development show that the effects of FDI are complex. FDIs are often regarded as generators of employment, high productivity, Competiveness, and technology spillovers from the macro point of view. FDI means higher exports, access to international markets and international currencies, being an important source of financing, substituting bank loans especially for less developed nations (Denisia, V, 2010). Foreign trade is the best way to participate in the world market, but the market perfection and no barriers in the terms of trade are needed for it. Hymer believes that always local firms will be better informed about local economic environment, and for foreign direct investments to take place, two conditions are necessary:

- foreign firms must possess certain advantages that allow them that such an investment to be viable;
- the market of these benefits has to be imperfect.

During the period of Second World War, international production was the small component of international affairs, but after that the attention was given towards foreign trade. Since 1960s, the concept of multinational corporations and FDI has started to gain importance. Ricardo's theory of comparative advantage was considered as the first attempt to explain FDI (Denisia, V, 2010). Some studies based on empirical data suggest that the integration of world economy with FDI and globalization improves the economic growth and development of developing nations and world welfare. Developing nations always like to attract direct investment from developed nation due to potential technology spillovers, because these nations believe that MNCs have high level of total factor productivity and hopefully MNCs would bring advanced technologies (Liu, Z, 2013). Due to technology spillovers and competition with MNCs the productivity and working efficiency of the company's of host country increased. The vital macro economic variables for the economic development of developing and developed nations are different depends on their factor endowment. The capability to attract foreign direct investment and its positive impact in emerging economies is valued as a vital part of the road to successful economic growth and development (Soonties et al, 2011). The domestic policy of the Government and the kind of FDI confirm the impact of FDI on the domestic country. FDI has two main effects on domestic economy, viz real effects and financial effects. Some effects are quantifiable like-income, employment, domestic investment, export growth, productivity & price level, but few can't be quantify. They are qualitative in nature, i.e the effect of FDI on structural changes, technology growth & spillover effects. With the injection of capital and technical know-how through FDI route certainly boost the strength of both transnational and local firms in the economy.

GOVERNMENT POLICY FORMULATION FOR FOREIGN DIRECT INVESTMENT IN INDIA:

In India, the Department of Industrial Policy & Promotion is the nodal Department for formulation of the policy of the Government on Foreign Direct Investment (FDI). To attract FDI and make this policy investor friendly, Government of India has put a liberal FDI policy. Under the liberal FDI policy, 100% FDI is permitted under the automatic route. To boost the manufacturing sector of India, the 'Make in India' global initiative was launched on 25th September 2014. Government has created a portal to promote India as a favored investment destination in the markets overseas and to increase Indian share of Global FDI. A number of FDI Policy reforms have been taken by the Government to open new sectors for FDI, simplify investment procedure, and ease of doing business. Policy reforms include increasing FDI limit up to 100% for trading, food products manufactured and produced in India, with 49% under automatic route in the Defense sector. The total FDI inflows in to India from 2000 to 2016 are US$ 457.35 billion (MOFPI, 2016-17). With a view to give impulsion to food processing industry, create enormous employment opportunities and benefitting farmers, 100% FDI under Government route has been permitted in respect of food products manufactured and/ or produced in India.

REVIEW OF LITERATURE:

Few studies have been developed on FDI inflows in food processing industries in India. So, a brief review of some studies on FDI in FPI is as follows.

Nunnenkamp, P & Spatz, J, (2003) analyzed that growth impact of FDI on the economic growth of host country is ambiguous. They showed the guaranteed positive growth effects of FDI. For US foreign direct investors, such data are provided in the BEA (2003) online data base, so they have used FDI stocks over FDI flows as this data is available for a large number of developing host countries. The authors had calculated standard regressions of lagged average annual growth rates of GDP per capita on the FDI-to-GDP ratio in 1990, on the basis of total FDI stocks and FDI stocks in the manufacturing sector, respectively. To check the growth impact of FDI, they have used average gross fixed capital formation, log GDP per capita, and secondary school enrollment in 1990, as well as three regional dummies for Latin America & Caribbean, Africa & Middle East, and Asia. The results of the study revealed that the link between FDI &economic growth is stronger in service sector than manufacturing sector. The growth effects of FDI also differ between manufacturing industries.

Mathiyazhagan , M., K. (2005) examined the long run relationship of FDI with the Gross Output (GO), Export (EX) and Labour Productivity (LPR) in the Indian economy at the sectoral level. The study used the Panel co-integration test (PCONT) on annual data from 1990-2001. The results of this study revealed that the FDI inflows helped to move up the output, labor efficiency and exports in some sectors. There is not a significant co-integrated relationship among FDI, GO, EX and LPR in sector hub.

Thanyakhan (2008), focused on the determinants of FDI and FPI in Thailand. Panel data is used to evaluate the results based on the data for time period 1980-2004 by using extended Gravity Model. The study also examined the effects of Asian Financial crisis of 1997 on the inflow of FDI and FPI in Thailand. The results of the study showed that the inflows of FDI in Thailand, which are supply-driven, are significantly influenced by its 21 largest investing partners. The 1997 Asian Financial Crisis has no impact on the determinants of the inflows of FDI into Thailand, but positively influences the inflows of FPI into Thailand.

Slimane, et al (2015) examined the foreign direct investments (FDI's) effects on food security. They have used panel data for 55 developing countries over the period 1995-2009 and build a composite indicator that synthesizes the food indicators used by the Food and Agriculture Organization to measure the food availability and food utilization. This study is based on model composed for food security equation and an agricultural production equation. Results of the research revealed that FDI in the agriculture sector have positive effect on food security and in the secondary and tertiary sectors have negative effects.

Srinivas, R, & Babu, T.K, (2017) observed the trends between gross capital formations of FPI & FDI flows in India and also analyzed the trends between FDI & FPI in India. The study has been based on secondary data, which has been collected from various governmental agencies like Annual Survey of Industries (ASI) reports, Ministry of Food Processing Industry (MOFPI), Department of Industrial Policy and Promotion (DIPP), and Ministry of Commerce. The researchers had used simple comparing methods to analyze the trends. The results of the study revealed that FDI inflows increased only in the second half of the 2000s to significant levels. However, the growth rates in FDI inflows fluctuated significantly. Infrastructural bottlenecks are primary reason for this shortfall of FDI inflows along with bureaucratic red-tapism, corruption and legal hurdles, policy uncertainty. These if addressed urgently would generate employment, boost the GDP growth and place India as the global food hub of the world.

OBJECTIVE OF THE STUDY:

To analyze the trends & pattern of foreign direct investment in Indian food processing industry.

DATA BASE AND RESEARCH METHODOLOGY:

Research Design:

Research design is a set of advance decisions that make up the master plan specify the methods and procedures for collecting, analyzing and interpreting the required data (Makwembere, 2014), there are two important research methods, quantitative and qualitative research methods. In the present study, an attempt has been made to analyze the trends & pattern of foreign direct investment in Indian food processing industry.

Data Source and Methodology:

In order to review the relevant literature, research papers have been collected from Global Investment Trends Monitor by United Nations UNCTAD, Reserve bank of India publications, World Investment Report by United Nations UNCTAD, Research Gate, referred journals viz. International journal, Internet research, European journal of Innovation, impact journals, international journal of research in humanities (IMPACT), international multidisciplinary research journal etc. these journals were from JSTOR, WILEY. These journals provide the commendable work which finally helps the researcher to conduct their research in expedient manner. The data about FDI in India is being published by the Department of Industrial Policy and Promotion (DIPP), the Reserve Bank of India. (RBI) and the Secretariat of Industrial Assistance,(SIA). These secondary sources consider the equity capital as Foreign Direct Investment; however the international Monetary Fund prescribes reinvestment and venture capital as FDI. In 2002, Government of India has redefined the FDI in India. Consequently, reinvestment and venture capital along with equity capital is being considered as FDI inflows (Sahoo, 2004). So according to the new definition, the data about FDI is available only after 2001. There is also discrepancy in the data given by alternative sources. This variation in FDI data by various agencies is due to inconsistency in defining FDI data. Few agencies consider American Depositary Receipts (ADRs) and the Global Depositary Receipts (GDRs) in the FDI inflows, but the RBI doesn't include ADR and GDR. The Reserve Bank of India considers American Depositary Receipts (ADRs) and the Global Depositary Receipts (GDRs) ion the portfolio investments.

Time Period of the Study:

The time frame of the study is 1991-2015. The Ministry of Food Processing Industry has come into existence in 1998. So to study the effect of FDI in the food processing sector, we have to compare divide data into two parts i.e. from 1991-2000 (Liberalization era- period I) and 2000-2015 (Liberalization era- period II) to compare the effects of FDI on FPI.

Table 1.1: FDI Inflows Into India (in `. Crores)

YEARS	Amount of FDI Inflows	% change in yearly FDI	FDI in FPI	Yearly increase in FDI in FPI (%)
1991-1992	316	-	2.12	-
1992-1993	965	205.37	82.22	38
1993-1994	1836	90.25	141.31	72
1994-1995	4126	124.72	199.61	41
1995-1996	7172	73.82	285.17	43
1996-1997	10015	39.64	832.29	19.2
1997-1998	13220	32.00	342.09	-59
1998-1999	10358	-21.64	94.75	72
1999-2000	9338	-9.84	444 .06	37
2000-2001	10733	14.93	198.13	-58

YEARS	Amount of FDI Inflows	% change in yearly FDI	FDI in FPI	Yearly increase in FDI in FPI (%)
2001-2002	18654	73.80	1036.12	422.94
2002-2003	12871	-31.00	176.53	-82.96
2003-2004	10064	-21.80	510.85	189.38
2004-2005	14653	45.59	174.00	-65.93
2005-2006	24584	67.77	182.94	5.13
2006-2007	56390	129.37	441.00	141.06
2007-2008	98642	74.92	632.00	43.31
2008-2009	142829	44.79	462.00	-26.89
2009-2010	123120	-13.79	1314.23	184.46
2010-2011	97320	-20.95	858.03	-34.71
2011-2012	165146	69.69	826.16	-3.71
2012-2013	121907	-26.18	2193.65	165.52
2013-2014	147518	21.00	2510.67	14.45
2014-2015	175886	19.23	3164.72	26.05
Total	1277663		17104.65	
Average	53235.96		712.69	
S.D	61448.417		821.62	
C.V (%)	115.42		115.28	
CAGR (%)	0.301		0.355	

Source: Compiled & computed from the various issues of RBI Bulletin, SIA Newsletters and www.kaavpublications.org.

Figure: 1

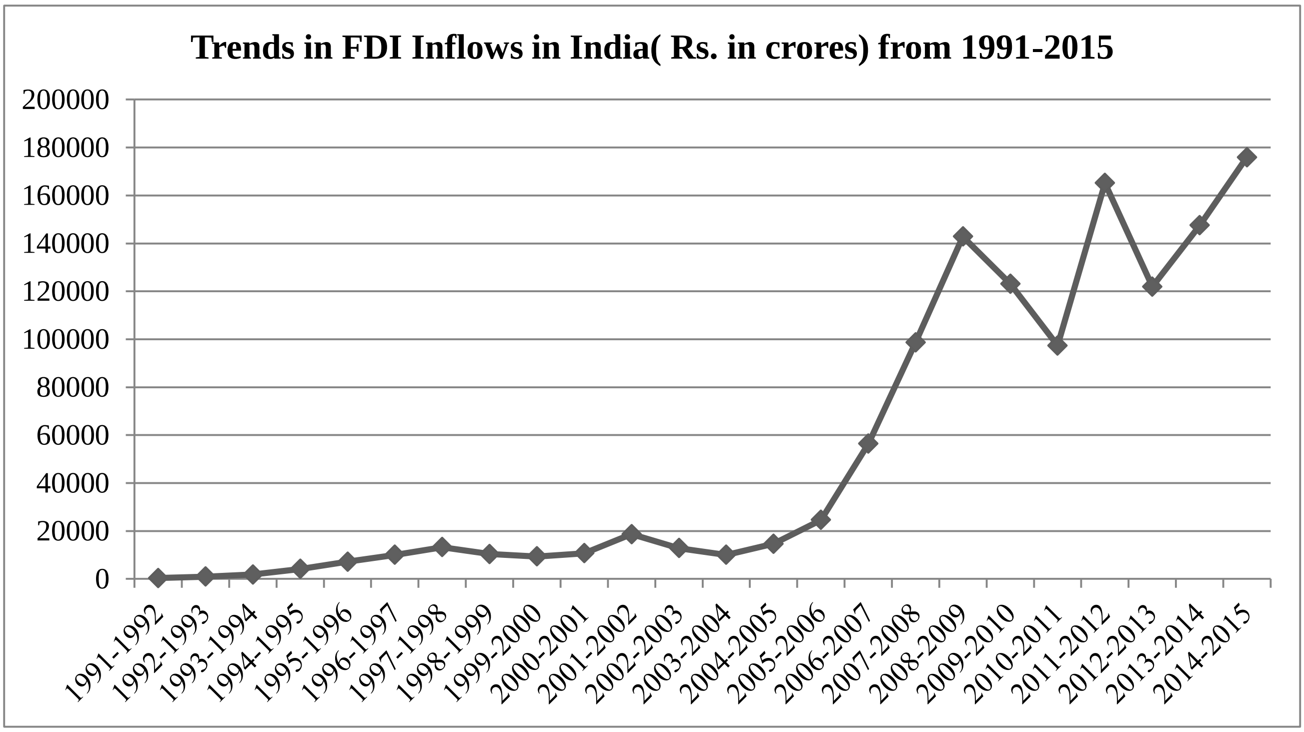
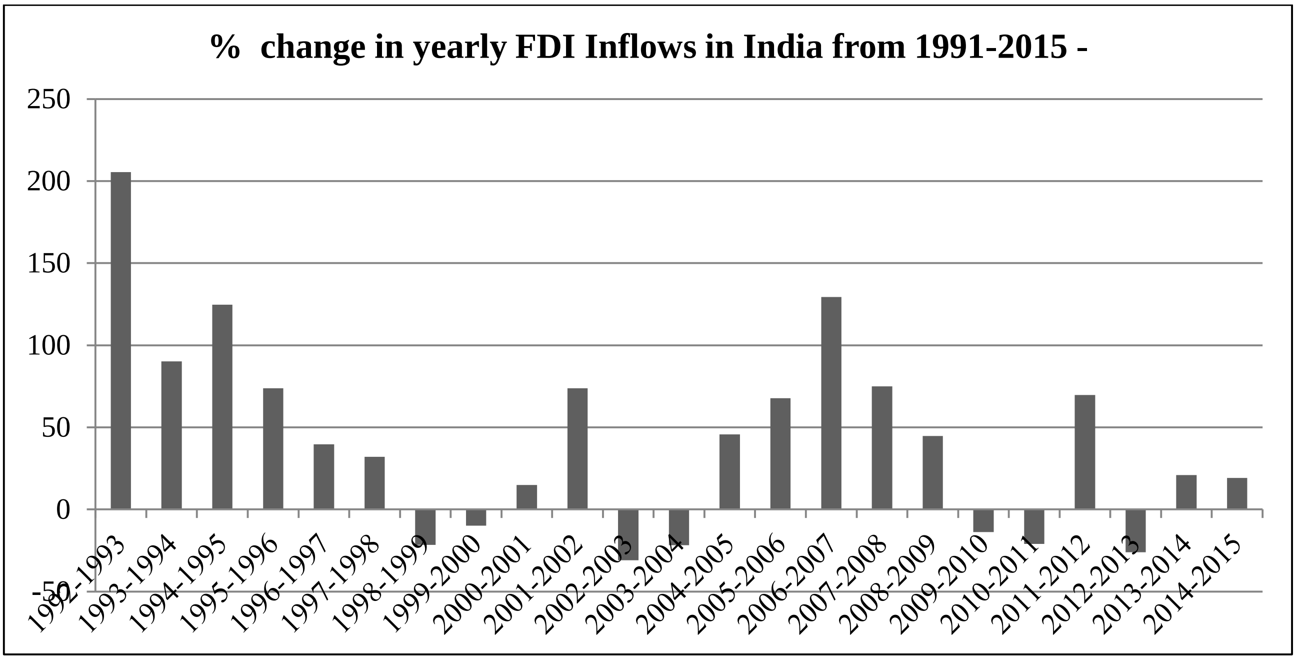


Figure: 2



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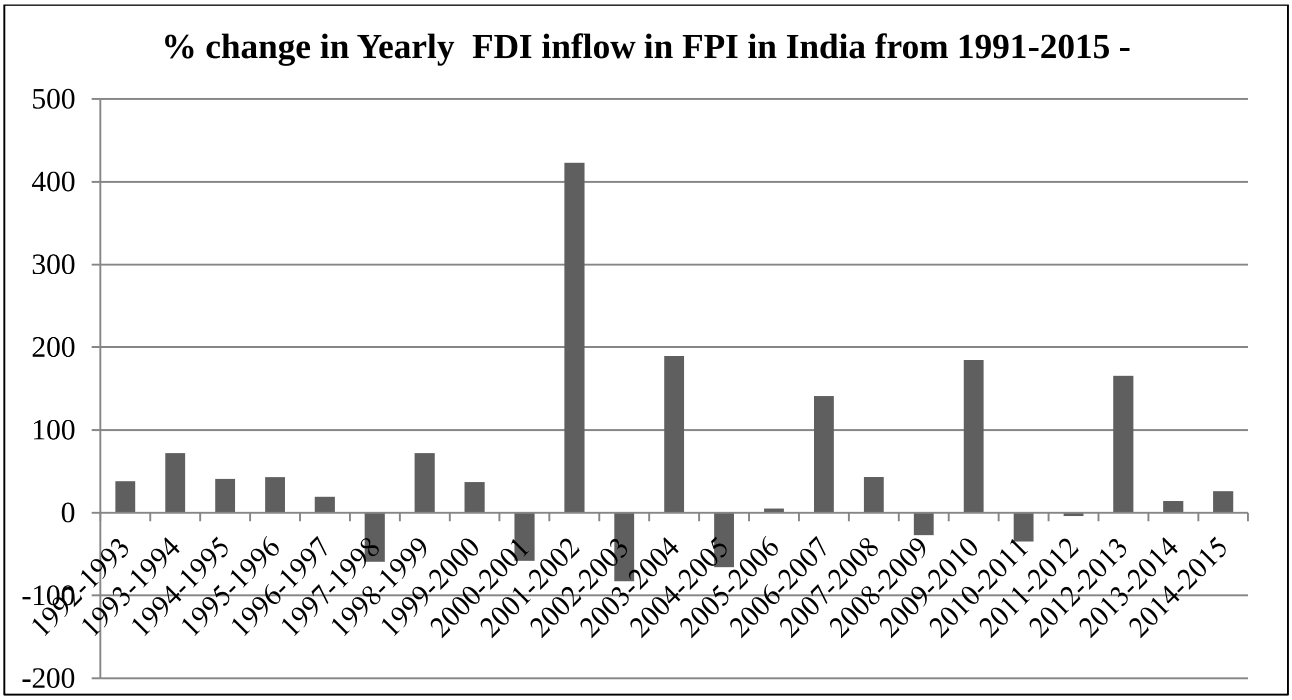


To know much about the FDI in FPI the method of Least Square has been used in the present study. With the help of the method of Least Square the trend values be calculated for the study period. The equation for calculating the trend values is

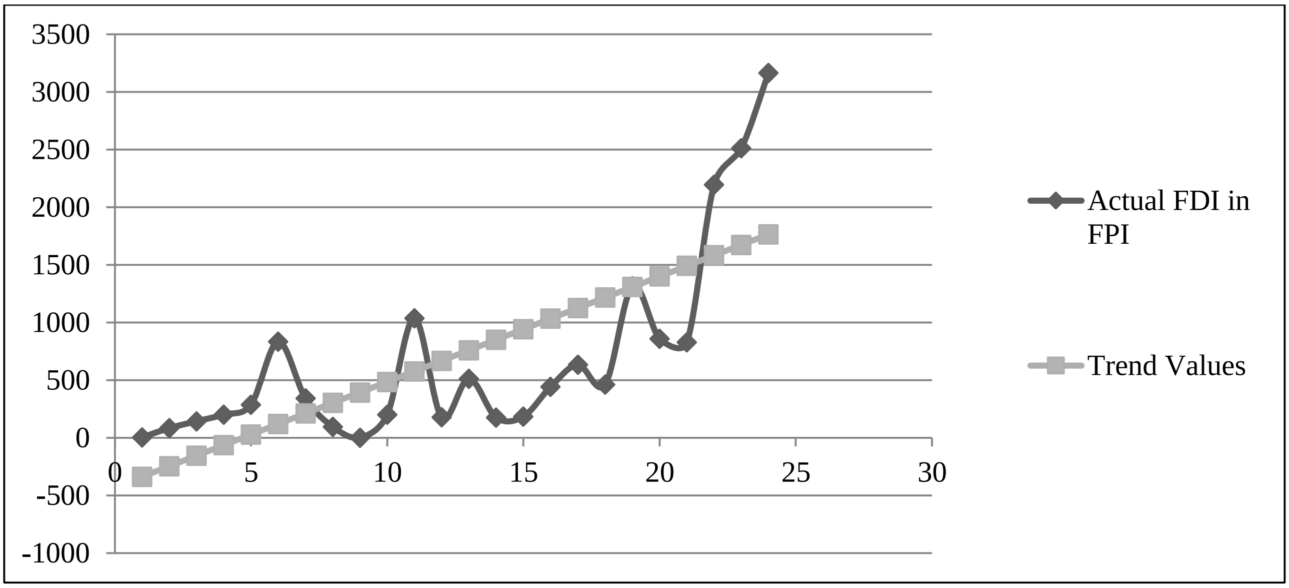
$$Yc = \alpha + \beta Xt$$

Where Yc =Trends in FDI Value
Xt = time period
α is the intercept and
β is the rate of change in Xt .
By using two normal equations the values of α and β has been calculated. and the equation with the values is $Yc = 484 + 91.5Xt$

Table 2: FDI in FPI (in ` Crores)

YEARS	Actual FDI in FPI	Trend Values
1991-1992	2.12	-339.5
1992-1993	82.22	-248.0
1993-1994	141.31	-156.5
1994-1995	199.61	-65.0
1995-1996	285.17	26.5
1996-1997	832.29	118.0
1997-1998	342.09	209.5
1998-1999	94.75	301.5
1999-2000	444 .06	392.5
2000-2001	198.13	484.0
2001-2002	1036.12	575.5
2002-2003	176.53	667.0
2003-2004	510.85	758.5
2004-2005	174.00	850.0
2005-2006	182.94	941.5
2006-2007	441.00	1033.0
2007-2008	632.00	1124.5
2008-2009	462.00	1216.0
2009-2010	1314.23	1307.5
2010-2011	858.03	1399.0
2011-2012	826.16	1490.5
2012-2013	2193.65	1582.0
2013-2014	2510.67	1673.5
2014-2015	3164.72	1765.0

Figure: 4



FINDINGS AND CONCLUSION:

Table 1.1 shows the FDI inflows and FDI inflows in the food processing sector of India from 1991-2015. The year wise FDI inflows in India and in FPI with the AGR and CAGR are also shown in the table 1.1. The coefficient of variation reflects the high variation in the inflows of FDI in India during 1991-2015 periods. The CAGR of FDI inflows in FPI is higher than the overall FDI inflows. The actual FDI inflow in to FPI in India improved from '2.12 crores in 1991-92 to the plane of '3164.72 crores in the year 2014-15.

The fig. 1 shows the FDI inflow into India from 1991-2015. After the new Economic Policy (1991) the FDI inflows into India has been increased, but this growth is slow up to 2005 and after 2006 there is a gradual increase. After 2009 there are cyclical variations in the foreign direct investment inflows in India.

Figure 2 shows the yearly percentage change in FDI inflows in India. There is negative growth rate in yearly FDI inflows during the period 1998-2000, 2002-2004, 2009-2011 and 2012-2013. The reasons behind the negative trend in FDI inflows were the political instability, the Gujarat earthquake (January 2001), terrorist attack on Indian Parliament (December 2001), the terrorist attack on the World Trade Centre (September 2001), which brought about a transitory disorder in the FDI inflows. In India FDI inflows were 205.37 per cent highest during 1992-93 followed by 129.37 percent during 2006-07 due to the back of positive investment environment, better growth scenario and initiatives intended at rationalized and liberalized FDI policy and simplifying the procedures.

The fig 3 shows the yearly change in FDI in FP sector of India from 1991-2015. The maximum growth percentage of FDI was recorded during 2001-02 in the Indian FPI.

Table 1.2 shows the trends in FDI inflows in to Indian FPI. During the period 1991-95 there was negative trend in FDI inflows. The trend value was decreased from -339.5 to -65.0 during 1991-1995, which is the positive indicator for the foreign investment in FPI. After 1995 the trend in FDI inflow in FPI was increasing.

After the existence of ministry of food processing industry and the implimentation of New Economic Policy the FDI in FPI has been increased, but with a very low pace. The FDI in food processing industry of India was maximum with the investment of 2193.65, 2510.67 and 3164.72 crores during the time period 2012-13, 2013-14, and 2014-15 respectively. The “Make in India” programme started by the government of India is the main initiative behind the maximum FDI 3164.72 crores in Indian food processing industry.

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