International Journal
of
Research in Finance and Management

P-ISSN: 2617-5754
E-ISSN: 2617-5762
IJRFM 2022; 5(2): 337-342
Received: 18-07-2022
Accepted: 21-08-2022

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An analytical study on the effect of COVID-19 on foreign direct investment (FDI) in India

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DOI: https://doi.org/10.33545/26175754.2022.v5.i2d.282

Abstract
The impact of the COVID-19 epidemic on remittance inflow to India is evaluated in this article. The influx of remittances has been significantly reduced because to this epidemic. To evaluate the short-, medium-, and long-term effects of COVID-19 on the Indian economy, a situation study was conducted using 2019-20 remittance data. This data was used to address the remittance inflow. Right now, the countries that provide money are all shut down, which has put a lot of people out of work. In particular, our analysis shows that COVID-19 had a negative effect on GDP, FDI, and unemployment via its effect on remittance inflow. Particularly hard-hit are emerging nations, as this trend is most pronounced in the primary and manufacturing sectors, which are the ones that get the lion's share of foreign direct investment.

Foreign direct investment (FDI), a key factor in economic development, may help nations weather the storm and recover stronger than before. Approximately three quarters of the foreign direct investment (FDI) inflows to the nation (from October 2019 to June 2020) went to only four Indian states: Maharashtra (28%), Karnataka (19%), Delhi (16%), and Gujarat (10%). This highlights potential opportunities for the other Indian states in the future. Low-skilled manufacturing received only 11% of all foreign direct investment (FDI) during the last 19 years, although India has great potential to attract big FDI in this area.

Keywords: GDP, COVID-19, FDI, development, Indian economy

1. Introduction

The global spread of the COVID-19 epidemic has caused several nations to reevaluate their economic policies. This is a similar period for India's economy, and FDI, or foreign direct investment, is likely to be a big part of it as it's a great way to fund growth without taking on debt. Over the years, the government has made concerted steps to create a foreign direct investment (FDI) policy that is both enabling and investor friendly. Total FDI inflows1 increased by 55%, or from US$ 231.4 billion in 2008-2014 to US$ 358.3 billion in 2014-2020, proving that the FDI reforms were successful. To sum up, foreign direct investment (FDI) fell more precipitously in 2020 than either global GDP or trade. Potentially detrimental effects include a decrease in investment capital due to the severity of COVID-19 in the home nation. Investors may not have the capital to invest overseas due to rising domestic company restrictions and the need to limit the loss of domestic operations. A smaller pool of investors is a result of this.

Reforms to attract investments and promote manufacturing in India have been a persistent emphasis of the Indian government. Things have been chaotic over the last few months. The dynamics of international commerce have been altered by trade wars and the subsequent COVID effect. Many companies have been reevaluating their risks and looking into new investment possibilities in light of this exceptional economic climate. The idea behind the CIIEY Survey came from a need to collect feedback from influential people at multinational corporations (MNCs) that are considering moving their assets to India or establishing new ones there because of the country's excellent investment climate. Also, we were hoping to find out what steps India may take to improve its performance for this.

Included in this study are the survey's findings and commentary from prominent EY and industry figures. Considering the global viewpoint, the respondents had a positive outlook on future investments. Over 80% of them want to make investments over the next two to three years. Positively, among the top three destinations for investments in the next two to three years, according to the respondents, is India.

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The three main reasons people choose India as a vacation spot are because of its stable government, large pool of qualified workers, and large potential market.

2. Review of literature

This part will evaluate relevant and related research to have a better understanding of the chosen issue, which is GDP, FDI, unemployment, and digital banking services, since these are the main points of the paper. Using panel data spanning 29 years, from 1970 to 1998, Chami *et al*. (2005) [8] found that remittances hinder GDP development across 113 nations. The researchers discovered that an increase in remittances had a dampening effect on economic expansion. They saw the function of remittances as philanthropic and not motivated by financial gain. Using System GMM panel data analysis, Rao and Hassan (2011) [5] examined 40 nations with high levels of remittance recipients. The specific result conveys both the direct and indirect impacts of remittances on development, as well as the mechanisms by which remittances could influence growth when treated as a conditioning variable. The research shows that remittances boost the ratio of M2 to GDP, which in turn helps the economy thrive.

Azam (2015) [1] looked into how remittances helped the economies of four countries: Sri Lanka, Bangladesh, India, and Pakistan, and they all came out ahead. Additionally, using the panel dataset of eighty-four nations spanning 1970-2004, Barajas *et al*. [2009] [2] found that remittances sent home by employees had little effect on GDP development in poor nations.

Using a panel data set spanning 1999-2013, Meyer and Shera (2017) [4] investigated the several effects of remittances on the GDP growth of six nations that receive large amounts of these funds: Albania, Bosnia Herzegovina, Bulgaria, Romania, Macedonia, and Moldova. The chosen six nations' GDPs have been positively and significantly boosted by remittances, according to the regression findings. Using panel data from seven CEE nations spanning 2010-2016, Comes *et al*. (2018) [3] elucidated the relationship between remittances, FDI, and GDP growth. For all of the states that were considered, the empirical results demonstrate that remittances and FDI contribute positively to economic development.

3. Objectives of study

- To understand the conceptual framework of COVID-19
- To study the impact of COVID-19 on FDI inflow

4. Key measures to attract FDI in India

India is set to become a top investment destination on a worldwide scale because to a number of structural reforms implemented by the government. These changes have targeted the land, labour, liquidity, and law sectors. Over twenty lakh crores of rupees have been pumped into the economy since the epidemic began. Power, manufacturing, defence, land, education, mining, and minerals are all included in the covered sectors.

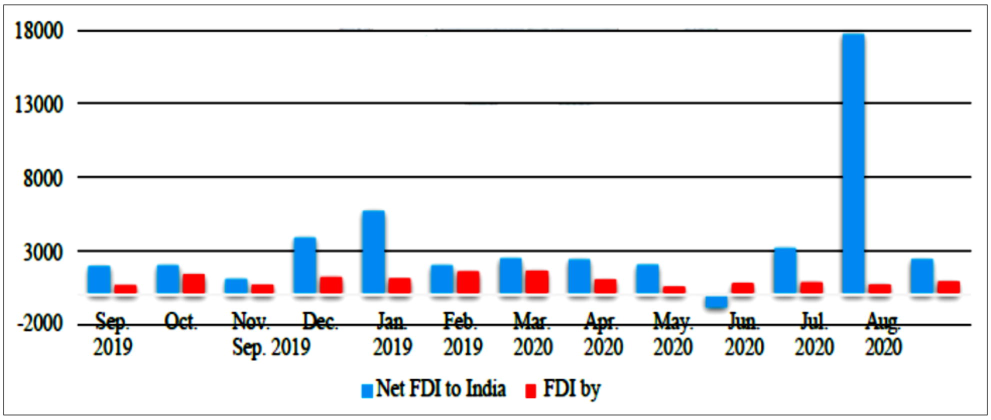
- The following are examples of significant changes that have taken place:
  Eliminating the Dividend Distribution Tax for corporations
- Setting the corporate tax rate for new manufacturing facilities at 15% to bring it in line with ASEAN nations
- A phased and graded tariff system to encourage domestic production of both intermediate and final items, such as electric vehicles.
- Thirteen industries would get production-linked incentives totalling Rs. 197,000 crores. Compensation for disabled workers in India's industrial sector in the form of monetary incentives based on incremental sales for five years. First priorities will include healthcare-related commodities and high-import items (cell phones).
- A rise from 49% to 74% in the foreign direct investment cap for military manufacturing via the automated route. To promote the expansion of micro, small, and medium-sized enterprises (MSMEs), we have:
- Streamlined more than 100 labor rules into 4 codes, making retrenchment exemptions more generous and reducing registration requirements The following are some of the recent developments in India:
- The opening of commercial coal mining and an integrated licensing regime for minerals mining • The Airport Authority of India (AAI) has awarded three airports out of six bids for
- Operation and Maintenance on Public Private Partnership (PPP) Basis
- The implementation of a GIS system to provide information on industrial land, including plot-level information
- The decriminalization of companies' law, the facilitation of netting of qualified financial contracts • The implementation of faceless e-assessment for taxes, the opening of commercial coal mining, and the establishment of an integrated licensing regime for minerals mining
  It is proposed to privatize the power departments and utilities in the union territories. As a result, Distribution's operations and finances will become more efficient, and other utilities throughout the nation will be able to follow suit.
- A new policy favouring public sector firms in some areas and the openness of all sectors to private sector. The industry and international agencies have long demanded changes pertaining to coal and mining, labour, agriculture, PLI & PMP, MSME, and corporate tax savings. Not only will these changes help the economy become more efficient with the resources it has, but they will also boost its productive capability.

5. Data Analysis: In the first three months of fiscal year 2020, foreign direct investment (FDI) equity inflows declined 62%, which contributed significantly to a 59% decline in Net FDI. Although stock inflows were down in the first quarter, they surged by 16% in the second quarter, attracting $20 Bn in equity FDI. This surge was driven mostly by tech investments from companies like Google, Facebook, Amazon, and others. While other capital flows decreased significantly from March to September (June being the only exception), reinvested profits hardly changed at all throughout that time.

Table 1: Impact of FDI Inflow

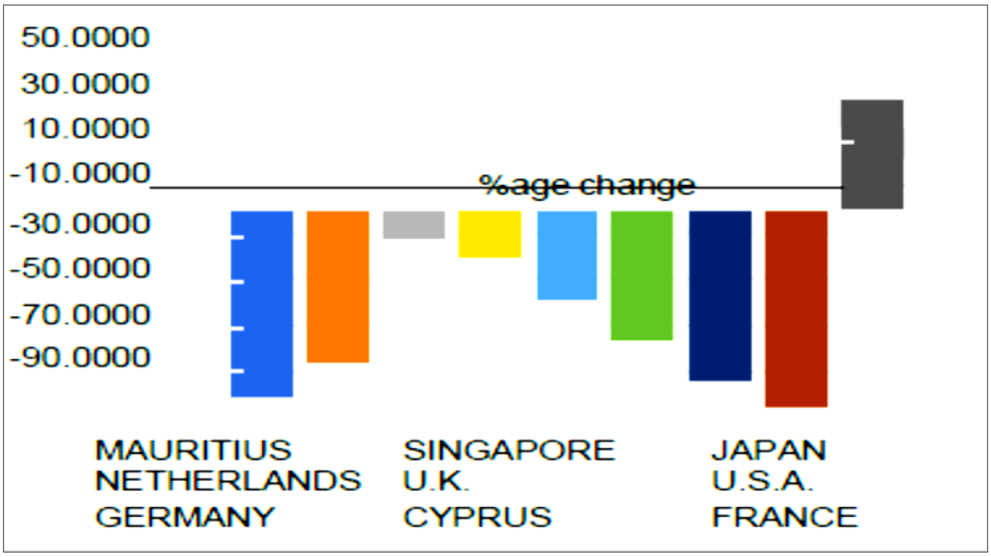
Year	2015	2016	2017	2018	2019	2017
FDI inflow	55559	60220	60974	62001	74390	67542

Source: RBI 2020, WORLD BANK 2020



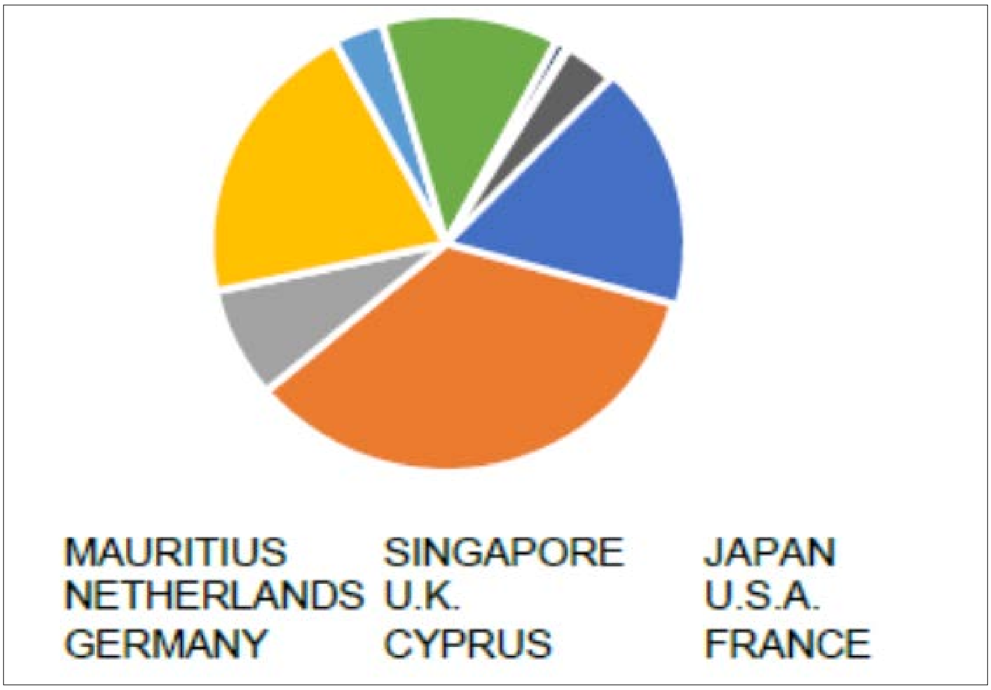
Source: RBI 2020, World Bank 2020

Fig 1: FDI Inflows vs. Outflows (in US $ million)



Source: RBI 2020, World Bank 2020

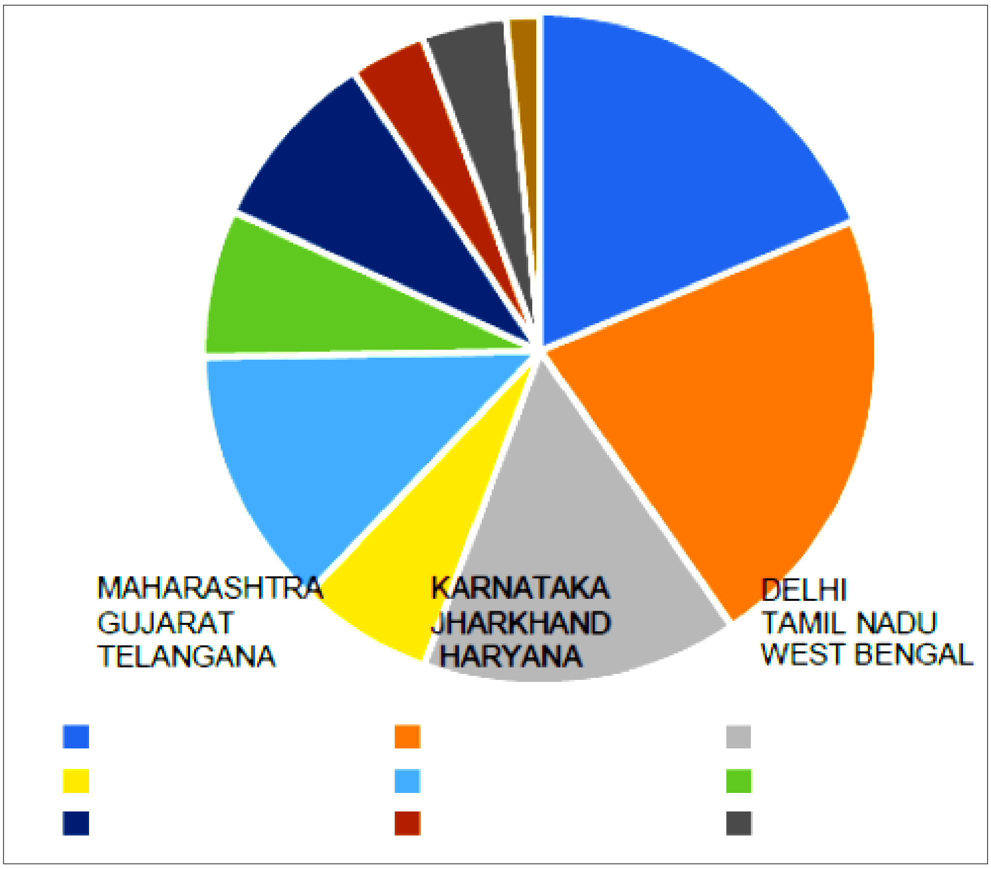
Fig 2: % change of Inflows during Covid-19



Source: RBI 2020, World Bank 2020

Fig 3: Contribution by country

For the first quarter of FY-20 most countries saw a major decline in their contributions towards equity inflows with Mauritius and Singapore falling by 80.7% and 65.8%, with only one exception France, which saw a growth in its contribution by 48.7%. Singapore emerged as the largest contributor of FDI bringing in $1.82 Billion followed by the Netherlands, Mauritius, the US, and Japan.



Source: RBI 2020, World Bank 2020

Fig 4: FDI Equity inflows by State 2020-21 (April - June)

During the first quarter of FY-20, the states which attracted the most FDI include Karnataka, followed by Maharashtra, Delhi, Jharkhand, and Gujarat. The states which saw the largest decline in FDI inflows include Delhi, Karnataka, Tamil Nadu, Gujarat and Andhra Pradesh.

Table 2: Regression Analysis

Summary output								
Regression Statistics								
Multiple R	0.9909476							
R Square	0.9819771							
Adjusted R Square	0.8668609							
Standard Error	575.94169							
Observations	12							
Anova								
	df	**SS**	**MS**	**F**	**Significance F**			
Regression	3	162658208.5	54219403	163.4548	1.62355E-07			
Residual	9	2985379.461	331708.8					
Total	12	165643588						
	Coefficients	**Standard Error**	**t Stat**	**P-value**	**Lower 95%**	**Upper 95%**	**Lower 95.0%**	**Upper 95.0%**
Equity	1.8147622	0.241502822	7.514456	3.64E-05	1.268444898	2.3610796	1.268444898	2.36107957
Reinvested earnings	-1.8149319	0.565259573	-3.21079	0.010645	-3.09363794	-0.536226	-3.09363794	-0.53622596
Other capital	-1.0896933	0.564072058	-1.93183	0.085421	-2.36571293	0.1863264	-2.36571293	0.18632636

Regression is a statistical method used to determine the dependence of a dependent variable on a group of independent variables. For our analysis we'll choose the variables as follows:

Y = dependent variable = Net FDI

X = independent variable = Equity, Reinvested Earnings and Other Capital After

Running regression, we get the following results:

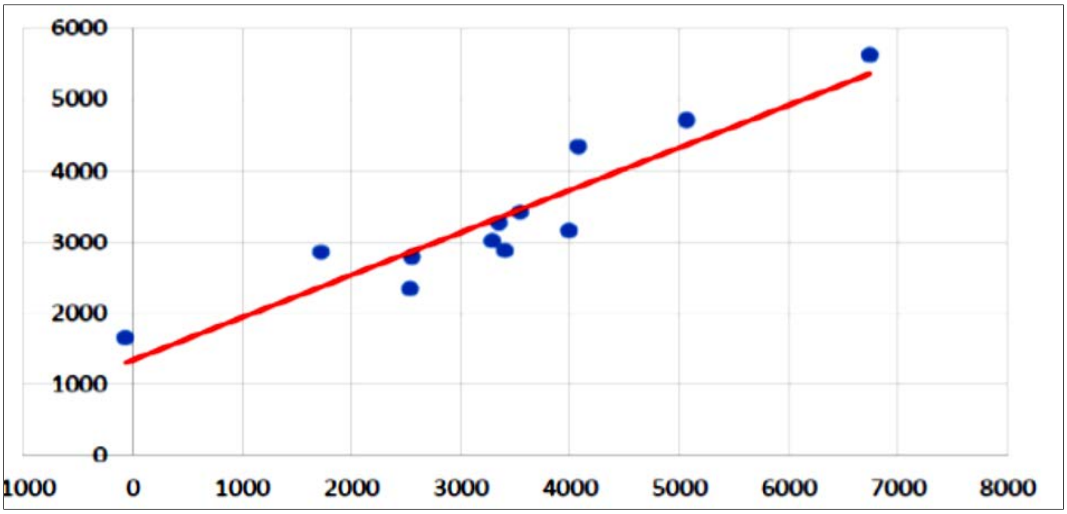


Fig 5: Line of Best Fit

6. Findings

R-Squared value is 0.9819 or 98.19%, which is a very good fit. This means that 98.19% of the of the variation in Net FDI can be explained by the chosen independent variables which are Equity, Reinvested Earnings and Other Capital.

6.1 F and P-values: Significance F is very small which means our result is statistically significant because the value is less than 0.05. P-value for Equity is very small which means Equity is a good fit (almost 100%) for Net FDI. For Reinvested Earnings, the P-value is 0.010645, which means we can say with 99% confidence that Reinvested Earnings is a good fit. For Other Capital P-value is 0.08542 which means this isn't significant as it is greater than 0.05.

6.2 Coefficients: Regression line is: Y = 1.8147*(Earnings) - 1.81*(Reinvested Earnings). From this equation we can say that for 1 unit increase in Equity, Net FDI increases by 1.814 units and for each unit increase in Reinvested Earnings Net FDI decreases by 1.8 units. From this equation we can also estimate any variable if we know the other two variables.

6.3 Line of best fit: This line of best fit expresses the relationship between the actual values and the estimated values. As the line obtained in our case is linear, we can say that the dependent variable varies linearly with the independent variable.

7. Indian economy: on the cusp of a major change

The India growth story in the last three decades is a story of constant renewal and finding new purpose to meet the goals and aspirations of a billion people. The Indian economy has evolved and made significant progress from a closed economy until the 90s to a vibrant economy of today. India stands at a critical juncture in the post pandemic world. Despite the headline news of 23.9% GDP contraction, Bank of America Research estimates that India's FY21 GDP is likely to contract by 7.5% and then roar back, in a U shape recovery, to 9% in FY22. We believe that India will become the world's third largest economy by 2028, overtaking Japan in nominal USD terms. Over the years, systematic reforms have helped the Indian economy withstand many a crisis. A few points on the Indian economy will illustrate the robustness of our economy.

India is confidently sitting on its highest foreign exchange reserves of US$ 573 billion.• India has the world's most liberal FDI rules with sectors like insurance, defence, single brand retail, food processing, smart cities and space technology opening up for foreign investment.

India now ranks 63rd out of 190 countries in World Bank's Ease of Doing business 2020 report. This has been possible as the government has continued to regularly review FDI norms, basis the changing economic landscape and geopolitical environment. All these proactive steps have borne fruit, as is evident from the ever increasing volumes of FDI inflows during 2020-2021 witnessed highest ever inflow of US$35.7 billion, a 13% increase from last year.

The post-COVID business environment presents much wider and deeper opportunities for interplay of foreign capital and Indian consumer markets. The grounds have already been set up, as a result of the Government's concerted drive towards greater digitization. Perhaps India has been ahead of the global curve both in terms of digital penetration and access to mobile first technologies. Even during the lockdown Reliance Jio raised US$20 billion in tech FDI, attracting the Godzillas of global tech— FB, Google, Intel, Qualcomm, apart from financial investors like Silver Lake, General Atlantic, KKR and several sovereign wealth funds.

8. Conclusion

We find that Greenfield foreign direct investment and cross-border mergers and acquisitions were immediately hit hard by the COVID-19 harm to the host country's industrial sector. Only Greenfield FDI was negatively affected by the host country's COVID-19 harm in the service sector. Additionally, Greenfield FDI in manufacturing was positively impacted by the home country's COVID-19 harm. Furthermore, we find that greenfield FDI was unaffected by the COVID-19 harm to the host nation, whereas M&A FDI in the service and manufacturing sectors were negatively affected.

Additionally, there are more immediate impacts of COVID-19 damage on FDI flows when we look at announced-based FDI flows, which could be withdrawn and not recognized later. Thus, foreign direct investment (FDI) flows have been complicated by the COVID-19 harm. This lines up with previous research on the intricate interplay between trade and foreign direct investment (FDI), which has focused on their complementary and substitutionary natures, respectively.

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