**International Research Journal of Marketing & Economics**
**ISSN (2349-0314) Impact Factor: 6.618**
**Vol. 10, Issue 01, January 2023**
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# A STUDY OF GLOBAL VALUE CHAINS IN FOREIGN DIRECT INVESTMENT IN INDIAN ECONOMY

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**ABSTRACT**

For the Indian economy to grow, foreign direct investment (FDI) is essential. Global value chains (GVCs), which are increasingly prevalent in FDI flows to India, have been on the rise recently. GVCs are the tasks that businesses complete in order to produce and offer a good or service to customers. These activities frequently include several nations, each of which specialises in a certain stage of the production process.. A significant source of funding for India's economic growth is foreign direct investment (FDI). In comparison to 2018, total FDI flows increased by 12 percent in 2019 to US $ 1,426 billion. FDI flows, which represented only 1.6 percent of GDP from 2015 to 2017 compared with more than 2 percent since the 2018. FDI reform was very low, remained incredibly low in 2019. Following the global financial crisis of 2008, FDI inflow decreased in 2018 and 2019, reaching their lowest levels since 2010. This article primarily focuses on the FDI situation in 2019 before many economies started to experience COVID-19 virus damage. Additional details on current FDI flows and projections by the end of 2021 are also discussed. The impact of COVID-19 on FDI flows is also discussed. Foreign companies directly invest in rapidly expanding Indian private enterprises. The Department of Promotion of Industry and Internal Trade announced on April 17, 2020 that India had revised its FDI strategy to protect Indian companies from opportunistic takeovers of Indian companies by virtue of the new COVID-19 pandemic. The new FDI Policy emphasizes that the Ministry of Commerce and Industry now closely examines all FDIs.

**KEYWORDS: Foreign Direct Investment, India, economic growth, international corporations, Indian enterprises**

# A STUDY OF GLOBAL VALUE CHAINS IN FOREIGN DIRECT INVESTMENT IN INDIAN ECONOMY

Global value chains (GVCs) have become an increasingly important driver of economic growth and development in recent decades. In India, GVCs have played a significant role in attracting foreign direct investment (FDI), which has helped to boost the country's manufacturing and services sectors.

Foreign direct investment (FDI) plays a crucial role in the development of the Indian economy. In recent years, there has been a growing trend of global value chains (GVCs) in FDI flows to India. GVCs refer to the activities that firms undertake to create and deliver a product or service to the market. These activities often span multiple countries, with each country specializing in a specific stage of the production process.

The study of GVCs in FDI in the Indian economy is important for several reasons:

Firstly, it helps to understand the nature and extent of integration between Indian firms and global production networks. This integration can facilitate technology transfer, knowledge spillovers, and productivity improvements in the domestic economy;

Secondly, studying GVCs in FDI can shed light on the drivers and determinants of FDI flows to India. For example, firms may invest in India to take advantage of its relatively low labor costs or to access its large consumer market. Understanding these factors can help policymakers design targeted strategies to attract more FDI and promote economic growth;

Thirdly, analyzing GVCs in FDI can provide insights into the distribution of value-added across different stages of production. This can help identify areas where India has a comparative advantage and can potentially move up the value chain. For instance, if India is primarily involved in low-value-added activities, policymakers can devise policies to encourage investment in higher value-added activities such as research and development or design;

Furthermore, study of GVCs in FDI can inform policy discussions on trade and investment linkages. By understanding how FDI and trade are interconnected through GVCs, policymakers can design policies that maximize the benefits from international trade and investment, such as export promotion or attracting investment in the export-oriented sectors

Lastly, analyzing GVCs in FDI can help monitor and evaluate the impacts of FDI on the Indian economy. This includes assessing the overall contribution of FDI to employment, innovation, and productivity growth. It can also help identify potential risks and challenges associated with GVC participation, such as labor rights violations or environmental degradation.

The strong business climate and the government of India's supporting policy framework ensure a continual infusion of foreign capital into the country. Over the past few years, the government has taken a number of actions, including easing FDI regulations in sectors like defense, PSU oil refineries, telecommunications, electricity exchanges, and stock exchanges. The government's attempts to make doing business easier and to reduce FDI restrictions are having an impact, according to the Department of Industry Promotion and Internal Trade. Between April 2000 and March 2020, India received US$ 469.99 billion in FDI equity. The largest inflows of US$ 7.85 billion in service equity, US$ 7.67 billion in computer and hardware, US$ 4.44 billion in telecommunications, and US$ 4.57 billion in commerce have been recorded by the services sector, according the 2019–20 data. India brought in the most foreign direct investment (FDI) equity from Singapore during the 2019–20 fiscal years, bringing in $14.67 billion USD, followed by Mauritius ($8.24 billion USD), the Netherlands ($6.50 billion USD), the United States ($4.22 billion USD), and Japan ($3.22 billion USD). In addition to being the main factor in economic growth, foreign direct investment (FDI) provided India's economic development with a sizeable non-debt financial aid. In order to benefit from India's relatively cheap labour and unique investment privileges like tax cuts, foreign companies invest here. The strong business climate and the government of India's supporting policy framework ensure a continual infusion of foreign capital into the country.

Strict public health precautions have been implemented by numerous governments to stop the COVID-19 pandemic from spreading. These public health initiatives caused serious economic disruptions, which had an impact on businesses' decisions about foreign direct investment (FDI). The governments have also implemented significant economic initiatives in an effort to prevent or cushion the negative economic repercussions of the public health crisis. Success determines how these public health and economic policy measures will affect FDI flows. FDI could be a significant economic supporter during the post-pandemic economic recovery. Evidence from previous crises has demonstrated that foreign affiliates, even small and medium-sized enterprises, can exhibit stronger resilience during crises because of their connections with and access to financial resources of their parent companies. Given that these economies were turning away from other international funding sources, such as portfolio investment, FDI may have been particularly significant for rising and developing economies. Regrettably, it seems that the pandemic is having a particularly negative impact on FDI flows to these nations. The pandemic has been especially severe on the primary and manufacturing sectors, for example, which account for a larger share of FDI in many of these countries than in the majority of developed economies.

- FDI may play a significant role during and after the crisis to aid economies, assist governments in combating the pandemic, and maintain contact with local businesses by assisting their affiliates financially.

- As a major portion of their FDI is accounted for by sectors that have been severely impacted by the epidemic, particularly the primary and manufacturing industries, FDI flows to developing nations are projected to fall even more.

- Even in the most positive public health scenario for 2020 and government economic support strategies to combat the COVID-19 pandemic and its subsequent recession, FDI flows are anticipated to fall by over 30%.

- If the public health initiatives and economic assistance programmes are unsuccessful, FDI flows could continue to fall below pre-crisis levels throughout 2021. FDI flows have been continuously declining over the previous five years.

## REVIEW OF THE WORKS ON FDI IN INDIA

Shilpi and Prasad (2007) have analysed that manufacturing and services have been the main sectors to utilise foreign investment. The study also looked at the areas where the government was subject to limitations, including agriculture, real estate, and rail transportation. Additionally, the government uses foreign investment and funds in certain economic sectors.

The relationship between FDI and the economic actors of the host country was highlighted as a spillover effect in the study by Dunning and Lundan (2008). The FDI has fueled industrial expansion in terms of new investment in the emerging industry.

According to Narayana (2012). The primary decision-makers are the key factors to increase foreign direct investment.

In their co-authored study Lall and Narula (2013) have highlighted the fact that with limited domestic resources, industrialization must rely more heavily on FDI. However, without indigenous competencies, FDI cannot propel industrial expansion.

In their co-authored article "Globalisation in the Indian Pharmaceutical Industry FDI spillovers and implications on Domestic Productivity: 1991-2007," Bajaj and Swastik (2017) had attempted to analyse and study the impact of globalisation on the pharmaceutical industry and FDI spillovers in various forms to the domestic pharmaceutical industry, among other things.

In their investigations, Rao and Ravikanth (2019) observe that the FDI primary driving force is to concentrate on large industrial units, public enterprises, job development, etc. It is stated that any foreign subsidiary or associate may be purchased by the investing corporation in the abroad zone. The corporation may make investments in a variety of areas to acquire shares.

Rena and Mbukanma (2022) in their jointly written research paper have analysed the FDI equity inflow during the Covid-19 outbreak.

**FDI flows could be impacted by divestments as well**

Global supply chains enable companies to quickly modify their operations to changing market conditions. A global survey conducted prior to the epidemic revealed that 84% of the enterprises surveyed anticipated carrying out similar activities in 2020–21, according to an OECD report. It is imperative to comprehend the dynamics of divestment, especially given the potential effects on the output of affected enterprises, the welfare of employees, and the well-being of communities. For instance, if formerly foreign enterprises that were sold off to their global parent could have even more devastating consequences on jobs and production in effective areas.

**FDI flow towards the end of 2021: Expected scenario**

Depending on how well economic and public health initiatives would perform during the second half of 2020, it was expected that the impact on FDI flows will vary dramatically. The most optimistic scenario predicts that income will start to rise by the end of 2021, when the economy starts to strengthen, in the second half of 2020, and that the proportion of direct investors who reinvest will likewise return to historical levels. It was also expected that nearly all of the pending M&A (Merger and Acquisition) transactions and the disclosed Greenfield projects would be finished. The lack of new investment agreements may cause a short-term downturn, but by the end of 2021, new investments are back to normal. As a result, it was anticipated that FDI flows would decrease from 30% to 40% in 2020 before increasing by a comparable percentage in 2021 to their pre-crisis levels. As it is mentioned above, it is crucial to remember that FDI flows have dropped since 2015 and have decreased more recently than at any other time since 2018 and 2019.

It was expected that the economic recovery would be uneven. While income will increase in some industries, it will remain below pre-crisis levels in others, and the fraction of income reinvested will increase slightly but not dramatically in all sectors. The ongoing M&A deals and the Greenfield initiatives will be finished, but additional investments will be foregone. The continuous drop in new transactions is reducing capital flows in addition to the absence of newly negotiated projects at this time. Other foreign acquisitions, however, might occur when more powerful financial firms purchase real estate at a discount. Reductions in equity capital flows would result from divestitures by financially challenged companies. These divestments will be necessary, even if the company is liquidated or sold off.

In the pessimistic scenario, capital flows are significantly reduced as many M&A transactions are pending, Among the Greenfield investments, fewer investments are completed as investor faces financial constraints. Earnings remain depressed across most sectors, and so does the share of earnings reinvested. Fighting corporations would be more likely to make divestitures, including more liquidation.

**The following are some recent significant FDI announcements:**

- Jio Platforms Ltd. sold 25.24 percent of its shares between April 23 and July 16, 2020, for a total of Rs 1.52 trillion (US$ 21.57 billion), in separate transactions with Facebook, Silver Lake, Vista, General Atlantic, Mubadala, Abu Dhabi Investment Authority (ADIA), TPG Capital, L. Catterton, Public Investment Fund (PIF), Intel Capital, Qualcomm Ventures, and Google.

- Philips, a Dutch consumer electronics and health technology business, said in May 2020 that it would invest Rs 250–300 crore (US$35.47–42.56 million) to expand its production and R&D facilities in India.

- Amazon India announced a $1 billion investment in January 2020 with the goal of digitising small and medium-sized enterprises and producing one million jobs by 2025.

- MasterCard stated in January 2020 that it will treble the amount of money it would spend on research and development in India over the following five years, spending up to $1 billion there.

- The largest foreign direct investment (FDI) in India's city gas distribution (CGD) sector occurred in October 2019 when Total S.A., a French oil and gas major, paid Rs 5,662 crore (US$ 810 million) for a 37.4% interest in Adani Gas Ltd.

- Reliance Industries (RIL) announced one of India's largest FDI agreements in August 2019 when Saudi Aramco agreed to purchase a 20% share in Reliance's oil-to-chemicals (OTC) business for an estimated $75 billion.

**Governmental Programmes**

- The government raised FDI in defence manufacturing under the automatic route from 49% to 74% in May 2020.

- In order to prevent opportunistic takeovers or acquisitions of Indian enterprises from surrounding countries, the government changed the existing consolidated FDI policy in April 2020.

- The government allowed non-resident Indians (NRIs) to purchase up to a 100% share in Air India as of March 2020.

- The government approved 26% FDI in the digital sectors in December 2019.

- In August 2019, the government approved 100% FDI via the automated route in open-sale coal mining (as well as in the construction of related infrastructure like washeries).

- The Government of India suggested opening FDI in the insurance, media (AVGC, i.e animation, visual effects, gaming and comics), and aviation sectors after consulting with all stakeholders in the Union Budget 2019–20.

**Insurance intermediaries are able to accept 100% FDI.**

By February 2019, the Indian government had been working on a plan to reach its target of attracting USD 100 billion in FDI.

A draft of e-commerce national strategy that aims to encourage FDI on the e-commerce marketplace model was announced by the Indian government in February 2019. Additionally, it asserted that the goal of the FDI e-commerce policy was to create a level playing field for all participants.

The Indian government aimed to promote and raise more money by using the Indian insurance intermediaries to account for 100% FDI.

FDI e-commerce legislation was modified by the Indian government in December 2018. The market-based e-commerce model allowed for 100% FDI, as per the updated legislation. Additionally, sales by any seller affiliated with an online marketplace or one of its group companies were restricted to a maximum of 25% of that vendor's overall revenue.

**Impact of a corona virus pandemic**

The Indian government passed an ordinance on April 18, 2020, shielding domestic companies from outside competition during the pandemic. The Ministry of Commerce and Industry reviewed all nations that share land borders with India prior to any FDI. India is the third-largest pharmaceutical market in the world in terms of volume and value. Between 2015 and 2020, the Indian pharmaceutical business will increase at a compound annual growth rate of 20%. In this industry, 74% FDI is permitted.

**In the First Half of 2020, FDI**

FDI was anticipated to decline significantly as a result of the pandemic, the resulting supply disruptions, demand contractions, and economic players' negative attitude. FDI flows were supposed to be immediately impacted by investment capital flows as merger and acquisition (M&A) and Greenfield acquisitions are halted. As corporations retain, equity capital flows was also expected to be impacted.

Reinvested income is now a part of FDI flows, which are becoming more significant and make up more than half of FDI inflows in 2019. Earnings from direct investment companies and the portion reinvested by the direct investor are the two criteria that determine the amount of returns reinvested.

A significant decrease in completed transactions was observed over the first quarter of 2020, according to the most recent data from the definitive report on cross-border M&As, although a rise in withdrawn deals is not depicted. Instead, the number of pending deals has grown. This indicates that direct investors have not attempted to undo their agreement thus far, instead appearing to be preventing them, mostly because to the difficulties of valuation in the current scenario. Since it is difficult and perhaps costly for them to withdraw from deals, as corporations would likely wait till economic developments take such a move in the near future. Due to too many deals, capital flows will decline temporarily, but when these deals are finished together with the stabilisation of the economy, they may indicate a future rebound. However, businesses that start to shut down may point to clauses that let the target companies to carry on with their regular operations until the purchase is finalised if the economy doesn't start to improve. Cross-border M&A is a particularly important factor in developed economies with more than three-quarters of completed cross-border M&A. On the other hand, greenfield investments often account for a larger portion of FDI in emerging and developing economies.

## CONCLUSION

The Make in India programme has greatly increased foreign direct investment (FDI) in India. From 2019 to 2020, FDI flows expanded astronomically especially in the manufacturing sector. The government's recent initiatives are to encourage and assist FDI in a number of areas. In India, foreign direct investment has grown significantly across a variety of economic sectors. FDI was attracted to India by the country's competitive investment environment, and that environment serves as the foundation for the company's growth. In order to improve the Indian infrastructure and raise the possibility of domestic absorption, certain important policy efforts are required. The best inflow and most effective driver of economic growth to benefit local businesses, improve macroeconomic conditions, and advance development will be FDI.
In conclusion, studying GVCs in FDI in the Indian economy is crucial for understanding the integration of Indian firms into global production networks, attracting more FDI, identifying comparative advantages, informing policy discussions, and evaluating the impacts of FDI. It provides valuable insights for policymakers, researchers, and businesses in their efforts to promote sustainable economic development in India.

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