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# FDI: A REAL BOOST TO GROWTH OF EMERGING ECONOMIES

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**ABSTRACT**

Increased availability of investable resources by foreign countries has led Foreign Direct Investment to become need of an hour. Emerging economies thriving towards achieving higher rates of economic growth are considering Foreign Direct Investments to be the best source of funds. OECD defines Foreign Direct Investment as "Foreign direct investment reflects the objective of obtaining a lasting interest by a resident entity in one economy (''direct investor'') in an entity resident in an economy other than that of the investor (''direct investment enterprise''). The lasting interest implies the existence of a long-term relationship between the direct investor and the enterprise and a significant degree of influence on the management of the enterprise. Direct investment involves both the initial transaction between the two entities and all subsequent capital transactions between them and among affiliated enterprises, both incorporated and unincorporated". Indian economy is one such economy which has shown increasing volume of Foreign Direct Investment amounting to US$ 44468 million till 2018. This research paper deals with relationship of FDI and GDP of BRICS economies. The regression analysis has been done to prove how closely Foreign Direct Investment is linked with Gross Domestic Product of BRICS nations. At the same time the paper has also focused on changes in FDI stocks, flows and Gross Domestic Product over the years.

**KEYWORDS**

BRICS (Brazil, Russia, India, China, South Africa), FDI (Foreign Direct Investment), GDP (Gross Domestic Product), Regression Analysis.

## 1. INTRODUCTION

Emerging economies are thriving towards achieving higher rates of economic growth. These nations consider Foreign Direct Investments (FDI) to be the best source to fulfill this objective. This research paper focuses on the contribution of FDI in the growth of BRICS economies. OECD defines Foreign Direct Investment as "Foreign direct investment reflects the objective of obtaining a lasting interest by a resident entity in one economy (''direct investor'') in an entity resident in an economy other than that of the investor (''direct investment enterprise''). The lasting interest implies the existence of a long-term relationship between the direct investor and the enterprise and a significant degree of influence on the management of the enterprise. Direct investment involves both the initial transaction between the two entities and all subsequent capital transactions between them and among affiliated enterprises, both incorporated and unincorporated." Empirical studies have also shown that Foreign Direct Investment (FDI) or stable, long term flows are more positively associated with growth through micro-linkages under certain conditions [1,2]. Developing economies are considered to be the best investment place as far as FDI is concerned. The availability of easy raw material, ease of doing business, man power, infrastructure, competitiveness, political and economic stability etc contribute to attractiveness of FDI in these nations. China and India are doing tremendously well to attract FDI where Brazil is doing good followed by Russia and South Africa to achieve higher rates of economic growth [3].

World Investment Report 2017 states that the BRICS nations contribute to 22% of global GDP and 11% of FDI inflows in 2016 [4]. India has also undertaken many reforms relating to FDI for ease of doing business and making India as attractive destination for investment by foreign entities [5]. Emerging Market Private Equity Association (EMPEA) in one of its survey stated 'India to be an emerging market for global partners' [6]. India is an attractive destination which can be seen by table 1 where even BRICS nations (except India) have invested in India in the form of FDI [7]. According to this table contribution of China is highest amongst these nations whereas Brazil has the lowest [8].

**Table1:** BRICS (except India) & FDI 2016 (Percent)

| Countries | In USD millions | Percentage contribution |
|---|---|---|
| Brazil | 24.83 | 0.01 |
| Russia | 1,234.54 | 0.35 |
| China | 1,738.98 | 0.49 |
| South Africa | 424.19 | 0.12 |

(Source: Quarterly Factsheet by Department Of Industrial Policy & Promotion 2017)

The Entry route of FDI (automatic/ government approval) depends on country, its norms and FDI policy it follows [9]. There are many sectors where FDI is either restricted or prohibited. For instance, in case of India atomic energy, lottery, gambling etc FDI is prohibited [10].FDI can either be in the form of FDI flows or stocks. Foreign Direct Investment flows and stocks have been depicted in table 2 and 3 which clearly indicates since post recession period FDI inflows are highest in China and lowest in South Africa. However, the year 2015-16 witnessed major change in respect of FDI flows in Russia [11]. As far as the FDI stocks are concerned the trend continues to be the same [12]. The impact of FDI on the growth of the emerging economies is witnessed in table 4.

**Table 2:** FDI Flows (in US$ millions)

| Countries | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 |
|---|---|---|---|---|---|---|---|---|---|
| Brazil | 45058 | 25949 | 83749 | 96152 | 76098 | 53564 | 73366 | 64291 | 57935 |
| Russia | 75856 | 27752 | 31668 | 36868 | 30188 | 53397 | 29152 | 11858 | 37176 |
| India | 43406 | 35581 | 27397 | 36996 | 23996 | 28153 | 34576 | 44008 | 44458 |
| China | 171535 | 131057 | 243703 | 280072 | 241214 | 290928 | 268097 | 242489 | 170557 |
| South Africa | 8172 | 8614 | 4015 | 3785 | 4403 | 8296 | 5772 | 1729 | 2270 |

(Source: OCED website)

**Table 3:** FDI (Foreign Direct Investments) (STOCKS) (in US $ millions)

| Countries | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 |
|---|---|---|---|---|---|---|---|---|---|
| Brazil | 260531 | 367183 | 640334 | 649131 | 675533 | 644837 | 614853 | 468671 | 625876 |
| Russia | 212887 | 367379 | 464228 | 408942 | 438195 | 471481 | 290054 | 264315 | 379329 |
| India | 125212 | 171218 | 205603 | 206373 | 224987 | 226549 | 265838 | 282609 | 318502 |
| China | 915524 | 1314771 | 1569604 | 1906908 | 2068000 | 2331238 | 2599102 | 2696344 | 2865941 |
| South Africa | 83649 | 138751 | 179564 | 159391 | 163509 | 152123 | 138904 | 126755 | 136837 |

(Source: OCED website)

The economic growth of these countries is indicated by their Gross Domestic Product in table 4. It is observed in the table that as far as the volume is concerned China ranks first amongst BRICS nations but in percentage terms the scenario is not the same, there India takes the lead.

**Table 4:** (Gross Domestic Product) (in US $ millions)

| Countries | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 |
|---|---|---|---|---|---|---|---|---|---|
| Brazil | 1695825 | 1667020 | 2208872 | 2616202 | 2465189 | 2472807 | 2455993 | 1803653 | 1796187 |
| Russian | 1660844 | 1222644 | 1524916 | 2051662 | 2210257 | 2297128 | 2063663 | 1365864 | 1283163 |
| India | 1186953 | 1323940 | 1656617 | 1823050 | 1827638 | 1856722 | 2035393 | 2089865 | 2263792 |
| China | 4598206 | 5109954 | 6100620 | 7572554 | 8560547 | 9607224 | 10482372 | 11064666 | 11199145 |
| South Africa | 287100 | 297217 | 375298 | 416878 | 396333 | 366810 | 351119 | 317611 | 235456 |

(Source: World bank website)

The present research paper has used the above data (2008-2016) for regression analysis as a major tool to correlate FDI and GDP for BRICS economies [13]. The two variables are FDI(X-Independent) and GDP(Y-Dependent). The regression equation will be: y=a + bx.
The results are given in table 5 and country wise analysis has been done in subsequent paragraphs.

## 2. ANALYSIS

**Table 5:** Regression Statistics

| *Regression Statistics* | Brazil | Russia | India | China | South Africa |
|---|---|---|---|---|---|
| **Multiple R** | 0.7879526 | 0.33706612 | 0.971528428 | 0.990976935 | 0.645524484 |
| **R Square** | 0.6208693 | 0.11361357 | 0.943867486 | 0.982035285 | 0.41670186 |
| **Adjusted R Square** | 0.5667078 | -0.0130131 | 0.935848556 | 0.979468897 | 0.333373554 |
| **Standard Error** | 254888.89 | 421379.934 | 88648.90651 | 364663.4982 | 47610.20477 |
| **Observations** | 9 | 9 | 9 | 9 | 9 |
| **Significance F/P value** | 0.0116669 | 0.37506829 | 0.00001247079 | 0.000000227751 | 0.060412989 |

FDI FINAL DATA.xlsx

### 2.1 China

FDI in China is known as RFDI (Renminbi foreign direct investment). Chinese economy has stepped up with many benefits which have attracted FDI [14]. The regression analysis is conducted for FDI and GDP data from 2008-2016 with the following results: The correlation coefficient is 0.990977. It shows there is a strong linear relationship between FDI and GDP of China where $r^2$ is 0.982035 which tells that this number of points fall on the regression line. Significance F level is negligible which means that the output could be obtained by chance is almost nil. It shows that there is strong correlation in FDI and GDP of China. The major factors contributing to increase in FDI includes competitiveness, capital availability, regulatory framework, stability, local Chinese market and business environment, openness to regional and international trade etc have attracted foreign direct investment.

### 2.2 India

In case of India it has been noticed that during reform period, FDI is considered the major source of non debt financial resource for development. The government foreign policy has also been favorable towards foreign capital inflows over the years. A regression analysis is conducted for FDI and GDP data (2008-2016) with the following results: The correlation coefficient in India is 0.9715284. It shows there is a strong linear relationship between FDI and GDP of India where $r^2$ is 0.9438675 .Significance F level is approximately negligible which means that the output could be obtained by chance is nil. Some of the reasons for such high correlation between the two may be attributed to favorable investment climate due to low wage rate, educated youth, special investment privileges like tax exemptions and ease of doing business [15].

### 2.3 Brazil

The analysis for Brazil indicates the correlation coefficient 0.787952617. It shows that in case of Brazil the same relationship between FDI and GDP continues [16]. The results are shown in table 2.0.The high correlation between FDI and GDP has been established in the economy due to the factors such as easy availability of raw material, domestic market of millions of inhabitants, geographic location and diversified economy which make Brazil as an attractive destination for FDI [17].

### 2.4 South Africa

As far as South Africa is concerned the correlation coefficient is 0.645524 [18]. It is noticed that there is also a linear relationship where $r^2$ is 0.416702 which tells that the number of points fall on the regression line [19]. But significance F level is approximately 6% which means that the output could be obtained by chance is 6%. It is observed that in case of South Africa correlation between FDI and GDP is not as prominent as it is in case of China, India and Brazil [20]. South Africa's economy attracts FDI because of its predominant demography, productive, diversified and advanced economy, abundant natural resources, transparent legal system and political stability. However some limitations like high crime rate, strikes, corruption, electricity supplies restricts the entry of free foreign capital inflows [21].

### 2.5 Russia

The correlation coefficient is 0.3370661 for Russia. It clearly indicates there is a linear relationship between FDI and GDP even for Russia where r2 is 0.1136136 which tells that number of points fall on the regression line [22]. However significance F level is approximately 37% which means that the output could be obtained by chance is 37%. The low correlation between the two (FDI and GDP) may be associated with the problems of investment climate in Russia. The major issues relating to external and internal factors such as management system, business culture and information system put adverse impact on the entry of FDI [23].

## 3. CONCLUSIONS

BRICS economies are heading towards higher levels of development in today's scenario where FDI is playing an important role for the growth of developing economies. This is witnessed by above analysis. In conclusion China ranks first followed by India, Brazil, South Africa and Russia in establishing a positive correlation between FDI and GDP respectively. Since the above statistics has clearly indicated that Foreign Direct Investment is an efficient and effective tool for promoting the higher rates of growth thus the countries should open the doors to enter, to encourage such type of investment. However, the areas where this type of investment should be allowed differ from time to time and from country to country. In view of the above analysis there are various reforms which are lined up by many economies to attract FDI in order to promote their economic growth. Such type of investment though contribute to the growth of the emerging economies, however the risk sharing is also very high and sometimes it may even result in financial crises. It is suggested that in order to reduce the higher risk sharing outcomes; institutional quality, systematic and disciplined macroeconomic policies and good governance should be observed by the countries.

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