

## Analysis of Foreign Capital and Foreign Investment in India

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### Abstract

*India made use of foreign investment after attaining independence in order to promote economic expansion and strengthen its balance of payments. It takes several forms, such as foreign investments, commercial borrowings and foreign aid. The level of total investment is increased and is complemented by FDI. It facilitates the efficient use of natural resources and enhances managerial and entrepreneurial skills. Market interest rates, which are higher than those for concessional loans classified as foreign aid are paid to foreign banks for commercial borrowings. From Rs. 897,744 crores in 2013–14 to Rs. 1,816,834 crores in 2022–23, the total amount of commercial borrowings has grown consistently, indicating a strong expansion in borrowing activity. India's foreign aid receipts have fluctuated significantly, peaking in 2020–21 with concessional loans. Over the years, FDI inflows have typically increased; the largest influx, of Rs. 396,955 crores, was reported in 2019–20. India's economic growth, industrialization, infrastructural development and general standard of living have all been greatly aided by foreign investment.*

**Key Words:** *Investment, Growth, Foreign Aid, Grants, Loans*

### Introduction

Foreign capital has significantly influenced India's economic development, beginning during the era of the East India Company. However, the British government's policies favored foreign capitalists while neglecting India's interests. After gaining independence, India utilized foreign capital to foster economic growth and improve its balance of payments.

Foreign capital refers to investments made by foreign governments, institutions, private individuals, or international organizations in another country. It encompasses various forms, including foreign aid, commercial borrowings, and foreign investments. Foreign aid can include grants and concessional loans. Investments are typically made in the form of foreign currency, machinery and technical

expertise. Foreign capital manifests in several ways, such as foreign

collaboration, loans in foreign currency, and direct foreign investments. While many foreign entities and governments provide grants, the key distinction is that loans should be paid back with interest, whereas grants don't require repayment.

### Need of Foreign Investment Foreign Capital in India

Foreign investment is not just a capital influx; it brings modern technology, managerial expertise, job opportunities and new markets for our products. It is vital, especially given the gap between our savings and investment needs, which can be bridged by foreign direct investment. Foreign investment is crucial for India's on the whole economic growth. Foreign Direct Investment (FDI) complements

domestic investment and raises the overall investment level. It improves managerial and entrepreneurial capabilities and enables the effective utilization of natural resources. FDI also supports the creation of risky, capital-intensive projects and drives advancements in technology. Additionally, it creates more job opportunities, fosters the development of basic industries and contributes to infrastructure development. Moreover, it helps mitigate foreign exchange shortages resulting from a deficit in the balance of payments.

Before Independence, the British government in India lacked a clear policy on foreign capital, favoring investments from British sources over those from other countries. Foreign capital significantly contributed to the development of railways, electricity, the jute industry tea and coffee plantations and coal and other mines in India. Following Independence, in 1948, the First Industrial Policy recognized the importance of foreign capital for the country's economic development. On April 6, 1949, Prime Minister Jawaharlal Nehru emphasized that India warmly welcomes economic assistance and technical cooperation from around the world, affirming that no discriminatory policies would be applied against foreign capital.

#### **New Foreign Investment Policy-1991**

The Foreign Investment Policy of 1991 was notably liberal, removing limits on foreign investment inflows. Previously, foreign equity participation was capped at 40 per cent, but it now allows for 100 per cent participation. While prior regulations required approval for all foreign investments and technology agreements, the new policy permits many investments under automatic approval. Additionally,

foreign capital is now accessible across all industries, not just capital goods and high-priority sectors, and significant incentives are offered to attract it.

The current stance welcomes foreign capital in both consumer and capital goods. FDI approvals are automatic, eliminating the need for prior government or RBI consent; investors only need to notify the RBI within 30 days of receiving investment. Previously reliant on foreign aid and commercial borrowing, India now welcomes various investment forms. The policy facilitates modern technology inflow by streamlining payment processes for foreign technical experts and testing indigenous techniques abroad. Indian companies can raise capital in international markets through instruments like GDRs, ADRs, and FCCBs. The government offers numerous incentives to draw foreign investment into projects of infrastructure like telecommunications, power and roads allowing 100% foreign involvement in joint ventures in these areas. The government grants automatic approval for FDI in select technologically advanced sectors, allowing 100 per cent foreign equity participation and enabling investors to repatriate their capital as desired. Under the new policy, FIIs can invest beyond the previous 24% cap with shareholder approval, provided they adhere to sectoral limits. By 2013, the number of registered FIIs in India had risen to 1,767. The government assures that foreign investments will be treated equally to domestic investments, with no discriminatory practices. Foreign investors can repatriate profits, dividends, interest, royalties, and fees, serving as a strong incentive for investment. The projects involving investments up to ₹5,000 crore require

clearance from the Foreign Investment Promotion Board (FIPB), which was eradicated in 2017. Now, approvals for such investments are handled by the relevant Ministry, while investments exceeding ₹5,000 crore need clearance from the Cabinet Committee on Economic Affairs. In summary, the new foreign investment policy is significantly more liberal and aims to encourage greater foreign investment in India.

**Objectives**

The primary objectives of this study are:  
 (i) To examine foreign investment and foreign capital in India on a year-by-year basis.

(ii) To appraise the necessity of investment and foreign capital in India.

(iii) To offer recommendations for the effective utilization of investment and foreign capital in India.

**Research Methodology**

Data related to commercial borrowing, foreign aid and foreign investment has been collected from Economic Survey 2023-24, Ministry of Finance, Government of India, New Delhi and Aid Accounts and Audit Division, Department of Economic Affairs, Ministry of Finance, New Delhi. The data has been used for calculating Compound

Annual Growth Rates (CAGRs), growth index of value and percentage share for the period from 2013-14 to 2022-23.

**Analysis and Discussion**

Foreign capital in India encompasses various forms of investment, including foreign direct investment (FDI), commercial borrowings and foreign aid. Foreign investment in India has seen significant growth, particularly in sectors like technology and manufacturing. Commercial borrowings have also increased, reflecting the country's expanding economic landscape. Foreign aid has shifted towards development projects, focusing on infrastructure and sustainability. The various types of foreign capital in India are outlined below.

**Commercial Borrowings**

Commercial borrowings are obtained from foreign banks at market interest rates, which are higher than those for concessional loans categorized as foreign aid. In recent years, the amount of commercial borrowings has significantly increased, contributing largely to the deterioration of our country's debt situation. Trend in commercial borrowing is clear from the Table-1.

**Table - 1**

**India's Outstanding Commercial Borrowings during the Period 2013-14 to 20122-23**

Year	Commercial Banks Loans	Securitized Borrowings	Loans/Securitized Borrowings etc., with Multilateral/Bilateral Guarantee + IFC (W)	Total Commercial Borrowings
2013-14	582644	313416	1684	897744
2014-15	635246	490895	2360	1128501
2015-16	647567	549076	2400	1199043
2016-17	567286	545906	2323	1115515
2017-18	550820	759701	2234	1312755
2018-19	659541	767283	2074	1428898
2019-20	823472	828604	2120	1654196
2020-21	806167	786907	1998	1595072
2021-22	793757	916492	1793	1712042
2022-23	874073	941018	1743	1816834
<b>CAGR</b>	<b>4.715</b>	<b>11.071</b>	<b>-1.729</b>	<b>7.515</b>

**Sources:** Economic Survey 2023-24; (Value in Rs. Crore)

Table-1 outlines India's outstanding commercial borrowings during the period from 2013-14 to 2022-23, broken down into different categories: commercial bank loans, securitized borrowings, and loans with multilateral/bilateral guarantees. Total commercial borrowings have steadily increased from Rs. 897,744 crores in 2013-14 to Rs. 1,816,834 crores in 2022-23, reflecting robust growth in borrowing activities. The commercial banks loans grew consistently, peaking at Rs. 874,073 crores in 2022-23, with a Compound Annual Growth Rate (CAGR) of 4.715%. The securitized borrowings showed strong growth with a CAGR of 11.071%, indicating a rising reliance on this borrowing method, peaking at Rs. 941,018 crores. And, loans with guarantees declined slightly over the period, with a negative CAGR of -1.729%, suggesting reduced reliance on this type of financing. The highest total borrowing occurred in 2019-20, followed by a dip in the subsequent year, possibly due to economic

conditions during the pandemic, before gradually recovering. The overall trend indicates a growing trend in commercial borrowings, particularly through commercial banks and securitized means, while highlighting challenges in utilizing loans with guarantees effectively. This reflects the evolving landscape of India's financing strategies over the years.

### Foreign Aid

India has received substantial foreign aid for development, which includes both loans and grants from abroad. Grants do not require repayment from the recipients, while the loan component consists of concessional loans provided by foreign governments and international organizations. Usually, foreign aid is given for definite uses only and receiving nation doesn't have the liberty to utilize it for other purpose. Data relating to foreign aid during the period 2013-14 to 2022-23 is clear from Table-2:

**Table - 2**  
**Amount of Foreign Aid Received by India during the Period 2013-14 to 20122-23**  
(Value in Rs. Crore)

Year	Concessional Loans	%age Change of Concessional Loans	Grants	%age Change of Grants	Total
2013-14	54372.6	99.742	140.2	0.257	54512.8
2014-15	48135.5	99.751	119.7	0.248	48255.2
2015-16	64208	94.613	3655.2	5.386	67863.2
2016-17	62650.4	99.603	249.5	0.396	62899.9
2017-18	61212.6	96.028	2531.4	3.971	63744.0
2018-19	96062.3	98.374	1587.6	1.625	97649.9
2019-20	75276.9	99.486	388.2	0.513	75665.1
2020-21	152149.9	99.914	129.6	0.085	152279.5
2021-22	104177.2	97.473	2700.3	2.526	106877.5
2022-23	106632.6	99.382	662.7	0.617	107295.3

**Sources:** Aid Accounts and Audit Division, Department of Economic Affairs, Ministry of Finance, New Delhi

Table-2 shows the amount of foreign aid received by India during the period from 2013-14 to 2022-23, detailing concessional loans, grants, and total aid. Notably, concessional loans peaked in 2020-21, reaching over Rs. 152,000 crore, with a significant increase in percentage change, indicating a spike in financial assistance during that year. Grants fluctuated more modestly, with a high in 2015-16. Overall, total aid increased over the years, especially in 2020-21, reflecting an ultimate reliance on foreign support during that period. The percentage changes in both categories illustrate varying trends in aid distribution, with concessional loans generally maintaining higher values.

### Foreign Investment

In the 1991 Foreign Investment Policy, the government began promoting foreign investment to reduce reliance on foreign debt. This investment primarily comes in the form of equity capital, which does not carry a fixed interest burden. Foreign investment refers to the capital put forth by individuals, companies or governments in assets or businesses situated in a different country. Foreign investment is often seen as a way to stimulate economic growth, create jobs and foster innovation in the host country. Inflow of foreign investment during the period 2013-14 to 2022-23 is clear from Table-3:

**Table - 3**  
**Foreign Direct Investment Inflows in India during the Period 2013-14 to 2022-23**  
**(Value in Rs. Crore)**

Year	Foreign Direct Investment (FDI)	Growth Index of Value
2013-14	186830	100
2014-15	215893	115.555
2015-16	294258	136.298
2016-17	283292	96.273
2017-18	253977	89.652
2018-19	301932	118.881
2019-20	396955	131.471
2020-21	406765	102.471
2021-22	418763	102.949
2022-23	335015	80.001

**Sources:** Economic Survey 2023-24

Table-3 presents the Foreign Direct Investment (FDI) inflows into India during the period from 2013-14 to 2022-23, value expressed in Rs. crore. FDI inflows have generally improved over the study period, with the highest inflow recorded in 2019-20 at Rs. 396,955 crores. The growth index indicates how FDI inflows have changed relative to the base year (2013-14, indexed at 100). For instance, in 2015-16, FDI inflows increased significantly, resulting in a growth index of 136.298. After peaking in 2019-20, FDI inflows

decreased in 2020-21 and again in 2022-23, with a notable decline in the latter year (index at 80.001). This suggests potential challenges in attracting foreign investment in the most recent years. The period from 2013-14 to 2018-19 showed a general upward trend, whereas 2019-20 to 2022-23 exhibited more variability, particularly the drop in 2022-23, which could be attributed to economic factors or changing investment climates. Overall, the table illustrates a growing trend in FDI over most of the decade,

with a notable peak and subsequent decline in the most recent years, reflecting a complex investment landscape.

### **Economic Development and Foreign Capital in India**

Foreign capital has been instrumental in driving India's economic development, fostering industrialization, enhancing infrastructure and improving the quality of life. While it presents challenges, the positive contributions of foreign capital are crucial for India's ongoing development journey. Foreign capital has made significant contributions to the economic development of India across various dimensions.

Modern technology plays a vital part in the growth of the Indian economy; however, much of the technology currently available is outdated and inefficient. The introduction of modern technology can be facilitated through foreign capital and aid, which often comes with technical expertise and trade experience. This advancement in technology boosts productivity, addressing the economy's pressing issue of inadequate capital that hampers growth. Since savings do not increase at the same rate as income, foreign capital fills this gap, making its role significant in enhancing capital availability. India has faced disequilibrium in its balance of payments, with imports growing faster than exports, leading to foreign exchange shortages. Foreign capital has increased the availability of foreign exchange, significantly aiding in this area. Additionally, the lack of essential economic and social infrastructure—such as railways, roads, canals, and power resources—has been a challenge, which foreign capital has helped to address, positively impacting agricultural and industrial growth.

Despite India's abundant natural resources, including minerals and water, inadequate capital and technical know-how have hindered their proper exploitation. Foreign investment can facilitate this process. Domestic private entrepreneurs are often hesitant to invest in basic industries and high-risk ventures, but foreign direct investment serves as venture capital, bridging this gap. This has led to the development of basic industries and risky sectors such as iron and steel, coal, oil exploration and energy generation, with foreign capital absorbing much of the initial risk. The influx of foreign capital has also spurred job creation, with many industrial units established through foreign partnerships and multinational corporations setting up operations in India. Additionally, foreign capital has enabled large-scale imports of essential goods, enhancing overall availability and helping to stabilize prices, even amid rising demand. To further its industrialization efforts, India needs to import capital goods like machinery and equipment, which can be challenging due to foreign exchange shortages. Foreign capital alleviates this issue by facilitating access to these essential imports. Given that India's export value is lower than its imports, boosting exports is critical and foreign capital can significantly contribute to this goal. Many foreign companies are permitted to establish operations in India with the stipulation that they export a certain percentage of their production, underscoring foreign capital's role in promoting exports.

### **Shortcomings of Foreign Capital and Foreign Investment**

- The influx of foreign capital and investment increases a country's reliance on others for machines, raw materials, and technical expertise.

- This dependency extends to the need for ongoing supplies of spare parts and technicians from those countries.
- Countries like India that receive foreign aid often must fulfill with the terms set by giver nations and institutions. This can restrict the receiver's capacity to apply independent monetary, fiscal, industrial and commercial policies.
  - The availability of foreign capital can negatively impact the growth of domestic financial resources. Easy access to foreign loans can reduce the incentive to increase local savings, which was particularly low in the early planning stages.
  - There is significant uncertainty associated with foreign capital and aid, as it can be withdrawn at any time. Consequently, foreign capital cannot be considered a permanent fixture in an economy, and its availability often diminishes during times of crisis when it is most needed.
  - Domestic producers may struggle to compete with industries funded by foreign capital, leading to decreased profits and potential production shutdowns, adversely affecting their growth.
  - External debt often poses a heavier burden than internal debt. Borrower countries must manage foreign exchange to meet their external debt obligations, and shortages can complicate repayment, including interest.
  - Foreign technology, which comes with foreign capital, can hinder the advancement of Indian technology and research. Indian firms reliant on foreign partnerships must depend on external sources for technical know-how and future improvements,

stalling domestic technological growth.

- In India, foreign capital tends to flow into high-profit sectors, resulting in inadequate development of essential and foundational industries. This leads to an imbalanced industrial landscape.
- Foreign loans create a debt servicing obligation, requiring repayment of both principal and interest after the loan period. The rising burden of debt servicing negatively impacts India's long-term balance of payments.
- Foreign aid is categorized into tied aid and untied aid. Tied aid is restricted to specific projects and must be used to purchase goods from certain countries, limiting the recipient's autonomy and often resulting in higher costs. In contrast, untied aid allows the borrowing country more discretion in its use. However, most foreign aid is not utilized freely.

### Recommendations

- Foreign capital should be directed toward productive initiatives that promote rapid economic growth. The income generated from these projects can be used to repay loans, making the foreign capital self-liquidating and less burdensome over time.
- India should seek more aid from international organizations like the International Monetary Fund, International Development Association and World Bank, rather than relying heavily on commercial loans. These institutions can provide untied, generous aid with minimal political pressure.
- Investment in export-oriented industries should be encouraged to

enhance foreign capital flow. Such investments would alleviate the burden of foreign capital while increasing the country's foreign exchange availability.

- Foreign loan agreements should ideally be long-term to reduce uncertainty and facilitate better planning for economic development. This approach would support investments in key long-term projects such as dams, irrigation systems, ports, and airports.
- For optimal use of foreign aid, it should be untied, allowing India to utilize it as needed. This flexibility enables the country to maximize the benefits derived from foreign capital.
- India should prioritize inviting foreign capital in the form of equity rather than loans. Equity investments carry enterprise risk without the fixed interest obligations associated with debt, making them a more favorable option.
- Efforts should focus on decreasing the burden of debt servicing. Encouraging concessional loans and seeking debt relief from international organizations can help manage this issue. Additionally, prioritizing the repayment of existing debts is essential.

In brief, while domestic investment is crucial for economic needs, foreign investment is also on the rise. Every effort should be made to encourage foreign investment, accompanied by necessary safeguards against potential negative impacts. To enhance the effectiveness of foreign capital and investment in driving India's economic growth, a balanced approach that incorporates both domestic and foreign investment strategies is essential. Implementing these recommendations can help safeguard

against potential drawbacks while maximizing the benefits of foreign capital influx.

### Conclusion

Thus, it can be concluded that the analysis underscores the pivotal contribution of foreign capital in economic development of India, highlighting its dual nature as both a catalyst for growth and a source of dependency. Foreign investment has not only provided essential capital and technological advancements but has also fostered job creation and infrastructure development. However, challenges such as over-reliance on external resources, potential negative impacts on domestic industries, and the burdens of debt servicing must be carefully managed. India's outstanding commercial borrowings show a steady increase, particularly in securitized borrowings, which have grown significantly. The reliance on traditional commercial bank loans remains strong, but the decline in loans with multilateral/bilateral guarantees suggests a shift in financing strategies. Overall, this indicates a growing capacity to leverage diverse borrowing sources. FDI inflows generally increased over the years, peaking in 2019-20. However, there is a noticeable decline in 2022-23, indicating challenges in maintaining foreign investor confidence and possibly reflecting broader economic uncertainties. This highlights the need for India to enhance its investment climate to attract and retain FDI. Foreign aid received by India has shown significant fluctuations, with a peak in concessional loans during 2020-21. This suggests a moment of increased reliance on external financial support, possibly due to domestic economic challenges. Grants have remained more stable but exhibit variations that reflect

changing priorities in international assistance.

To maximize the benefits of foreign capital while mitigating risks, India should adopt a balanced strategy that emphasizes productive investments, prioritizes equity over debt and encourages export-oriented industries. Seeking aid from international organizations can offer more flexible financial solutions. By addressing these challenges and implementing strategic recommendations, India can harness foreign capital effectively, driving sustainable economic growth while safeguarding its autonomy and fostering domestic innovation. This balanced approach will be essential for navigating the complexities of a globalized economy and ensuring long-term development.

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