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Impact of COVID-19 on foreign direct investment in India: An analytical study

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Abstract
This paper assesses the effect of COVID-19 pandemic on the inflow of remittance in India. This pandemic has effectively been declined remittance inflow. Situation investigation is determined on remittance of 2019-20 to address the inflow of remittance for assessing the effect of COVID-19 on the economy of India for short, medium, and long period. At present, the remitter nations are locked down, made individuals jobless. This examination demonstrates the adverse consequence of COVID-19 on remittance inflow, precisely on GDP, FDI, and Unemployment. The developing countries are hit even worse because the sectors attracting the largest shares of FDI such as primary and manufacturing sectors are hit the worst. FDI being a critical driver of the economic growth could play an important role in supporting the economies during and after the crisis.
Four Indian states- Maharashtra (28%), Karnataka (19%), Delhi (16%) and Gujarat (10%) - attracted around 3/4th of the FDI inflows in the country (from October 2019 to June 2020), highlighting areas of opportunity going forward for the rest of the Indian states • Only 11% of total FDI in the last 19 years was in low skill manufacturing, highlighting the potential for India to attract large FDI in low-skilled manufacturing sector.

Keywords: Unemployment, GDP, COVID-19, economy, opportunity

1. Introductions
The COVID-19 pandemic has led to a reset in the economic strategy of many countries across the world. India too is going through such a phase, and Foreign Direct Investment (FDI) will play a significant role in this economic strategy as an important source of non-debt finance for economic development. The Government has taken determined measures over the years to provide an enabling and investor friendly FDI policy. The FDI reforms have borne positive results, as is evident from the fact that total FDI inflows1 grew by 55%, i.e. from US$ 231.4 billion in 2008-14 to US$ 358.3 billion in 2014-20. Thus, in 2020, global FDI decreased more considerably than global gross domestic product or trade. The severity of COVID-19 in the home country can also have a negative impact by reducing investment capital. Investors may face increased business constraints at home, need to minimize the loss of home business and thus may not afford to invest abroad. This reduces the number of investors.
India has consistently focused on reforms for attracting investments and encourage manufacturing in India. The last few months have been tumultuous. Trade wars, followed by the COVID impact, have changed global trade dynamics. In such an unprecedented economic environment, many businesses have been reassessing their risks and exploring new opportunities for investments. It is in this context that the CIIEY Survey was conceptualized - to gather response from key decision makers for those MNCs seeking to relocate investments or making fresh investments in India if they find it as an attractive destination for investments. We also wanted to explore how India can raise its game for the purpose.
In this report, you will see insights from some of the leading minds in EY and the industry, as well as the results of the survey. From a global perspective, the future investment outlook of the respondents is encouraging, with more than 80% of them planning to make investments in the next 2-3 years. Encouragingly, for the respondents, India is amongst the top 3 choices for future investments in next 2-3 years. While choosing India as their favored destination, market potential, skilled workforce and political stability are the three biggest attractions.

2. Review of literature

Since the paper focuses on GDP, FDI, Unemployment, Digital banking service, this section will review the appropriate and related studies to get a better idea of the selected topic.

Chami *et al*. (2005) [9] included 113 countries in their research and concluded that remittances have a negative impact on GDP growth using panel data of 29 years over the period 1970-1998. They found a negative correlation between the remittance's growth and economic growth. They identified the role of remittances as an altruistic which is not profit driven.

Rao and Hassan (2011) [6] conducted a study on 40 high remittance recipient countries using a System GMM panel data analysis. The exact outcome communicates the direct growth effects of remittances and the growth effects of the channels through which remittances may affect growth by treating as conditioning variables. The study finds that remittances indirectly facilitate economic growth by increasing the ratio of Broad Money (M2) to GDP.

Azam (2015) [4] examined the role of remittances in fostering economic growth in Bangladesh, India, Pakistan and Sri Lanka and found the positive impact of remittances on economic growth in all countries. Besides these studies, Barajas *et al*. [2009] [5] concluded that workers' remittances do not have any impact on economic growth in developing countries by employing the panel dataset of 84 countries over the period from 1970 to 2004.

Meyer and Shera (2017) [3] studied the various impacts that remittances have on the economic growth of six high remittances receiving countries, Albania, Bosnia Herzegovina, Bulgaria, Romania, Macedonia and Moldova using panel data set over the period 1999-2013. Regression results show a positive and significant contribution of remittances in the economic growth of the selected six countries.

Comes *et al*. (2018) [2] explained the connection between remittances, foreign direct investment, and economic growth, using panel data from seven countries from Central and Eastern Europe covering the period 2010– 2016. The empirical result show the positive effect of remittances and foreign direct investments on economic growth for all selected states.

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

The Government has undertaken several structural reforms with a focus on land, labor, liquidity and law that will globally position India as an attractive investment destination. Since the onset of the pandemic, it has injected over Rs. 20 lakh crores stimulus for the economy. The sectors covered include power, manufacturing, defence, land, education, mining and minerals.

4.1 Some of the important reforms that have been put in motion are

- Corporate tax rate for new manufacturing facilities at 15% to make it competitive vis-à-vis ASEAN countries.
- Abolition of Dividend Distribution tax on companies.
- Phased and graded duty structure to incentivize indigenous manufacturing of intermediate and final goods e.g., Electric Vehicles.
- Production linked incentives of Rs. 197 thousand crores for 13 sectors.
- Monetary incentives on incremental sales for a period of five years to offset disability manufacturing in India. Initial focus on high import items (cell phones) and healthcare related products.
- Increase in FDI limit for defence production under automatic route from 49% to 74%.
- Expanded the definition (turnover and investment thresh holds) of MSMEs to encourage MSMEs to grow.
- Consolidating over 100 labour laws into 4 codes with higher exemptions for retrenchment and fewer registrations implementing a GIS system to provide information on industrial land include plot-level information.
- Enabling ease of doing business through faceless e-assessment for taxation, decriminalization of companies' law and allowing for netting of qualified Financial Contracts.
- Opening of commercial mining of coal and integrated licensing regime for minerals mining.
- Airport Authority of India (AAI) has awarded 3 airports out of 6 bids for.
- Operation and Maintenance on Public Private Partnership (PPP) Basis.
- Power Departments/ Utilities in Union Territories to be privatized. This will improve operations and financial efficiency in Distribution and provide a model for emulation by other utilities across the country.
- New Public Sector and Enterprises Policy where all sectors are open to private sector while public sector enterprises will play a role in defined areas
- "Atmanirbhar Bharat Rozgar Yojana" launched to incentivize creation of new employment opportunities during the COVID recovery phase.

The reforms related to corporate tax cuts, labour, agriculture, PLI & PMP, MSME, coal and mining etc. were the long-pending demands of the industry and multilateral agencies. These reforms will help in increasing not just the productive capacity of the economy, they will also make the economy more efficient in use of the resources available.

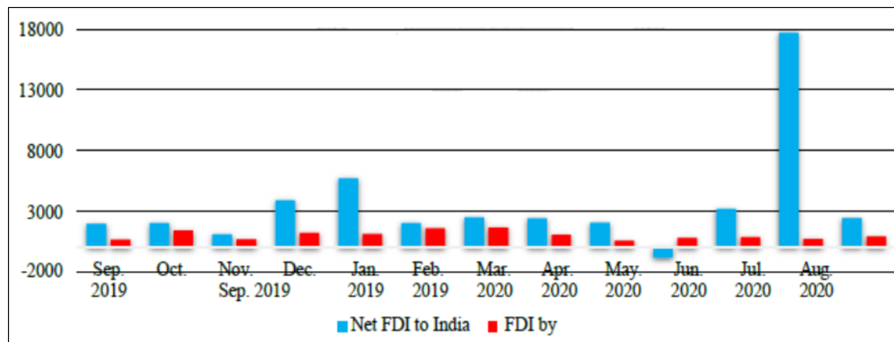
5. Data Analysis

For the first quarter of the FY-20, FDI equity inflows dropped by 62% and as they form a major portion of the Net FDI, Net FDI fell by 59%. Equity inflows dropped in the first quarter and saw a steep rise of 16% in the second quarter bringing in $20 Bn of equity FDI which was mostly fueled by tech investments by Google, Facebook, Amazon and such. Reinvested earnings saw little to no change from March to September, whereas other capital flows gradually declined from March to September with an exception for June.

Table 1: Impact of FDI Inflow

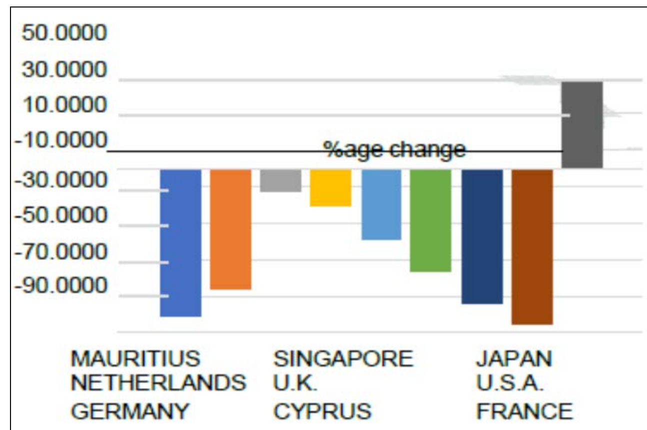
Year	2015	2016	2017	2018	2019	2020
FDI Inflow	55559	60220	60974	62001	74390	67542

***Source*:** RBI 2020, World Bank 2020



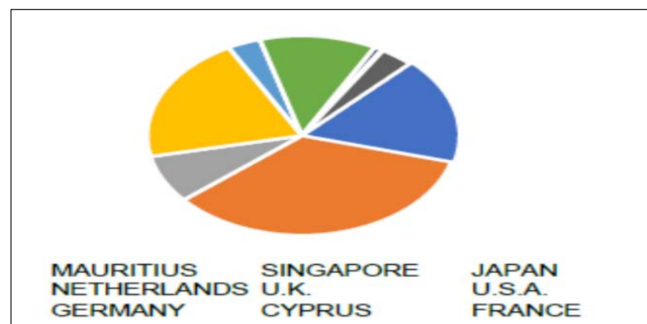
Source: RBI 2020, World Bank 2020

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



Source: RBI 2020, World Bank 2020

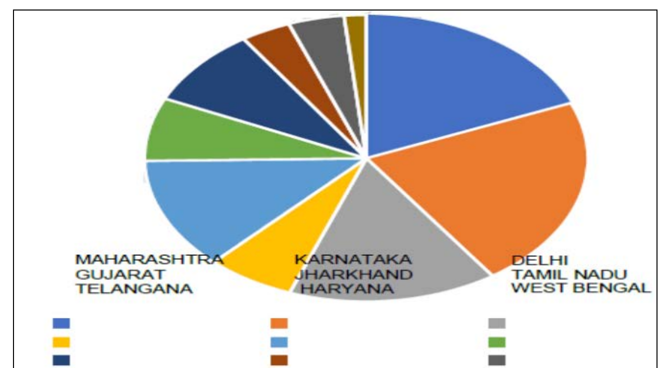
Fig 2: % change of Inflows during Covid-19



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	515.94169							
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 Star**	**p-value**	**Lower 95%**	**Upper95%**	**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:

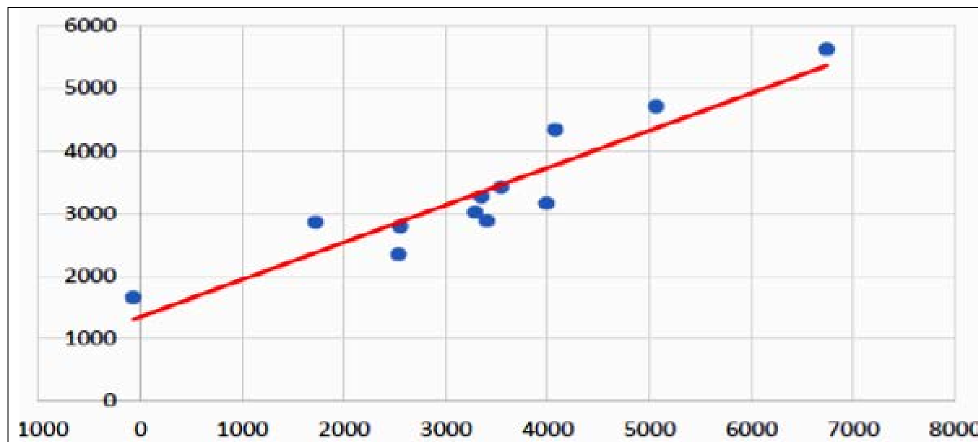


Fig 5: Line of Best Fit

6. Findings

6.1 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.

6.2 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.

6.3 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.

6.4 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, in the case of the manufacturing sector, the host country's COVID-19 damage had an immediate negative impact on Greenfield FDI and cross-border M&A. In the service sector, the host country's COVID-19 damage had a negative impact only on Greenfield FDI. Moreover, the home country's COVID-19 damage had a positive effect on Greenfield FDI in the manufacturing sector. We also find that the host country's COVID-19 damage had a negative lagged impact on M&A FDI in both the manufacturing and service sectors, whereas there was no such lagged impact on greenfield FDI.

Furthermore, when we examine announced-based FDI flows, which may be withdrawn and not realized later, we find more instantaneous effects of COVID-19 damage on FDI flows. In summary, COVID-19 damage has had complex effects on FDI flows. This is consistent with the past literature on the complex relationship based on substitution between trade and FDI on one hand and complementarity on the other.

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