IMPACT OF A COUNTRY'S INDUSTRIAL POLICY ON A FIRM'S FOREIGN DIRECT INVESTMENT DECISION

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THIS study examines the impact of industrial policy on foreign direct investment decisions of firms investing in India. The industrial policy factors considered are the tax reforms, and the procedural and administrative aspects of industrial policy. Personal interviews were conducted on select firms in Singapore having investments in India, their joint venture partners across India and certain experts. The latter were academics and government officials drawn from various organizations and institutes in Singapore and India. The study has revealed that the industrial policies of the Indian government have been important in influencing a firm's foreign direct investment decision. There were various aspects of industrial policy, which the firms considered significant, viz., the procedural and administrative aspects of the policy. The procedural aspects of industrial policy refer to the procedures the firms have to follow to obtain approvals and to begin operations. The administrative aspects of industrial policy refer to the percentage equity holding being allowed, and the ability to repatriate the capital invested or the profits earned. The Indian bureaucracy was the main stumbling block which deterred investors from considering any further operations in India. The experts ascribed this solely owing to the mindset of the bureaucrats and the investors. The firms interviewed stated that they would continue their investments in India.

Introduction

India has steadily been increasing its trade with other countries and attracting more foreign investments since the launch of its economic reforms in 1991. These reforms have involved the opening of the economy for international competition, making it more competitive, getting the government out of the huge morass of regulation, empowering the States to take more responsibilities for economic management and thereby creating competition between the states for foreign investors. There has been an increase in the GDP rates over the past few decades. During 1991-92, the GDP growth rate which had collapsed to 0.8%, rebounded to an average rate of 7.5 % between 1994-1997 and stabilised at around 5.5% in 2000. There was an increase in the average growth rate to 6.9% in the years between 1994-1998 when there was a slow down, as compared to 5.6% during the 1980s. This positive trend in the growth rates occurred in most sectors and it was able to neutralise the debilitating effects of several state and national elections, the East Asian economic crisis, the Kargil operations, the nuclear explosions, and the US sanctions that followed.

Liberalisation of the foreign direct investment policy regime has resulted in a substantial expansion of foreign direct investment approvals and flows. Cumulatively, FDI approvals between April 1991 and September 1998 were of the order of $54,268 million and actual FDI was $11,806 million. As a proportion, actual FDI was 21.7% of approved FDI (Table 1). Although a little daunting, it is necessary to look at the increase in foreign direct investment in India *per se* since liberalization. From the Table 1, it can be inferred that there was a substantial increase in foreign direct investment from 1991 to 1998.

This difference in the amount of approvals and the actual flows of foreign direct investment was clearly articulated by the then Prime Minister, Mr H.D. Deve Gowda, "Something must be wrong with India" (*The Straits Times*, 17/10/96).

Table 1: Foreign Direct Investment: Actual Inflows vs. Approvals

	1991	1992	1993	1994	1995	1996	1997	1998	1991-98 Total
Approvals US $ Mn.	325	1781	3559	4332	11245	11142	15752	6132	54268
Actual Inflows US $ Mn.	155	233	543	958	2100	2383	3330	2073	11806
Actual as % of Approvals	47.7	13.1	16.1	22.1	18.7	21.4	21.1	33.8	21.7

Note: *Figures are up to November 1998.*

Source: *Government of India, Economic Survey 1998-99.*

India: The Pre – 1991 Era

At the outset, it is important to note that India is no stranger to liberalization. Two minor efforts at reform, one during the late 1970s under the leadership of Prime Minister Mrs. Indira Gandhi and the other during the mid-1980s under the prime ministership of her son, Mr. Rajiv Gandhi were attempted. Prior to 1991, India had managed to sustain its level of economic growth only through borrowing from abroad. Foreign investment was not welcomed. Noisy rows with multinationals like the Coca Cola and the IBM, both of which were ejected from India in 1977, were only the most prominent symbols of how unwelcome foreign investors were in India, and how unappealing India was to them. The three pillars of the pre-1991 system (Rohwer, 1995) were a high degree of government ownership of industry (and later entire government ownership of banks), a high degree of government regulation of privately owned industrial business and the screwing down of foreign trade (later just imports) and foreign investment to the lowest possible level.

India: The Post – 1991 Era

The New Economic Policy adopted by the government of India in June 1991, was based on the twin principles of deregulation of the government's interventionist function's and encouraging competition. The thrust of this policy was to ensure free flow of investment, production, technology and managerial personnel across national borders leading to greater integration of the Indian economy with the rest of the world. Various Indian regulations in the areas of Industrial Licensing, Monopoly and Restrictive Trade Practices and Foreign Exchange Regulations have been changed extensively to augment the pace of liberalization and deregulation.

The liberalization efforts of the Indian Government as initiated in 1991 have included: (1) the abolition of industrial licensing for all industries except those reserved for the public sector for strategic and safety reasons such as arms, ammunition and defence equipment; (2) granting of automatic approval for FDI between 51%-100% of equity in certain industries, for units set up in Export Processing Zones (EPZs) or those which are 100% "Export Oriented Units" (EOUs) subject to specific norms. There has also been an attempt to streamline the entire approval process so that a foreign investor may obtain approvals more expeditiously to commence investment and business in India. Various agencies have been set up for the processing of foreign direct investment applications. This includes the Foreign Investment Promotion Board (FIPB), and the Secretariat for Industrial Assistance (SIA), and the Foreign Investment Implementation Authority (FIIA). The procedures for FDI approvals were also made simpler allowing for more transparency.

As part of the above liberalization process, the policy makers have also attempted to reorient India's international relations, particularly its economic relations towards countries in Asia and the Pacific. For example, India is a sectoral dialogue partner of the Association of South East Asian Nations (ASEAN), with the sectors being trade, investment, tourism, science and technology. Malaysia and Indonesia along with India belong to a Group of 15 (G–15) major developing nations, with a combined Gross Domestic Product (GDP) of US$1.4 trillion and a total trade turnover of US$400 billion. Besides strengthening bilateral relations with the countries in the region, India has also expressed interest in joining the Asia Pacific Economic Cooperation grouping.

Literature Review

Various theories have examined "how", "when" and "where" approaches of FDI. The "how" approach was contained in the work of many celebrated authors who stated that firms undertaking FDI operated in an imperfect market environment, where it was necessary to acquire and sustain certain net advantages *vis–a-vis* firms in the country in which they operate. The second approach tries to answer the question: "why" firms produce in one country rather than another. The pioneering works on American Industry in Europe followed this approach, as did the authors of most of the early case studies published between 1953 and 1970. In most cases, the influences on location were extracted from field study data and occasionally ranked in significance. Later, when complete statistics were available, regression analysis was used to identify the main factors leading to US investments across Europe and Canada.

For the most part, these two approaches to explain international production evolved independently of each other and for this reason, if not for any other, neither was wholly satisfactory. The industrial organization approach did not answer where ownership advantages were exploited; likewise, the location theory approach did not explain how it was that foreign owned firms could outcompete domestic firms in supplying their own markets. Nonetheless, neither approach attempted to explain the dynamics of foreign investment. To the questions "why" and "where", Vernon (1979), added "when" to the theory of foreign investment. But even the Vernon theory(1979) was initially put forward to explain the growth of US manufacturing investment abroad, and during the 1960s at least, relied exclusively on data about US corporate activity.

All the three aspects, however, were treated independently. The eclectic theory by Dunning (1980, 1988, 1993), integrated the three strands of economic theory explaining the ability and willingness of firms to serve markets and the reasons why they chose to exploit this advantage of foreign production rather than domestic production, exports or portfolio resource flows. The principal hypothesis of Dunning's eclectic theory is that a firm will engage in FDI if three conditions are satisfied. They are: the firm possesses net ownership advantages *vis–a-vis* firms of other nationalities in serving particular markets. These ownership advantages largely take the form of the possession of intangible assets, that are, at least for a period of time, exclusive or specific to the firm possessing them; it must be more beneficial to the enterprise possessing these advantages to use them itself rather than to sell or lease them to foreign firms that is, for it to internalize its advantages through an extension of its own activities rather than externalize them through licensing and similar contract with independent firms and it must be profitable for the enterprise to utilize these advantages in conjunction with at least some factor inputs (including natural resources) outside its home country; otherwise foreign markets would be served entirely by exports and domestic markets by domestic production. The eclectic theory assumes that the greater the ownership advantage of enterprise (net of disadvantage operating in a foreign environment), the more the incentives they have to exploit.

The eclectic paradigm has been used in many studies and in various different ways. It has been used to explain investment in the non-manufacturing sector/service sector and manufacturing sector, investments in other countries, India included, and the choice of entry mode.

Kumar (1994) in examining the determination of export orientation of foreign production by the US multinationals used the location advantages in the eclectic theory and classified the factors as structural and policy factors. The structural factors identified by Kumar (1994) are: cost of labor, quality of industrial infrastructure and associated services, availability of experienced and skilled manpower, and the quality and quantity of natural resources. The policy factors looked at are the provision of export-processing zones, tariff and non-tariff incentives, performance requirements, and pollution requirements. The classification of location advantages into structural and policy factors is useful as it helps to see the effect of policy factors against the total effects of structural factors in a country.

The findings of Kumar's study (1994) concluded that export oriented investments were special types of FDI. Hence, a more specific targeting is important on the part of developing countries seeking such investments. Kumar's study (1994) of export oriented investments showed that such investments were the primarily driven by availability of low cost of resources, human as well as material. In contrast, other studies on market oriented investments showed that income levels, market size and its growth rate, the levels of urbanization and political stability determine such investments. (Root and Ahmed 1978, Schneider and Frey 1985). As there is an intense rivalry among countries to attract export oriented investments; multinational enterprises are more selective and tend to pick up winners among competing countries (Kumar,1994). Countries which succeed are generally those providing MNCs with established infrastructure, skills and further incentives in export processing zones besides low cost resources.

Loree and Guisinger (1995) examined the effect of policy and non-policy variables on the location of new US foreign direct investments abroad, as distinct from reinvested earnings on existing affiliates using the 1970 and 1982 benchmark data. Location determinants were divided into policy and non-policy variables. The policy variables considered were performance requirements, investment incentives and tax rates. The non-policy variables were political stability, cultural distance, market characteristics, availability of infrastructure and wage levels. This study concluded that although policy variables were important because governments could alter these quickly while it took years to alter non–policy determinants, such as market size and infrastructure, as the mere raising of incentive levels will not increase the amount of foreign investment. An increase in investment may bring about adverse effects. Countries which employ incentives often overshoot the mark, creating waste through redundant incentives; money spent on infrastructure may yield more results than if spent on incentives and the trigger effect that is, when one country increases its incentives, other countries may do the same resulting in no country increasing its relative share of foreign direct investment.

Root and Ahmed (1978) studied the effects of policies of host developing countries aimed at attracting FDI in the manufacturing sector. The factors included were economic, social, political and policy factors. Policy factors included taxation, tax incentive laws – their complexity, simplicity and liberty, local content requirements, attitude towards joint ventures and limitations in foreign personnel. Political stability factor included the frequency of government changes, number of internal armed attacks, degree of nationalism and per capita foreign aid from US and non–US sources. It was concluded that government policy had no bearing on FDI. If foreign investors regard a country's investment climate as poor, then liberal policies on joint ventures, local content requirements and limitations of foreign personnel are unlikely to improve it. Tax incentives and concessions are not effective to attract FDI as most countries provide similar concessions and incentives.

India: A Case in Point

The case of FDI in India does not fit exactly into either the theory or the literature discussed so far. The policy factor considered in past research includes the effect of tax and non-tax incentives and the repatriation of profit and capital restrictions on foreign direct investment. India is peculiar in various ways. Policy in India has a much wider meaning than normal parlance. We think it is necessary to consider industrial policy from two aspects: administrative and procedural aspects. The administrative aspect of policy refers to the amount of equity that a foreign investor is entitled to have in an investment and the form of investments allowed that is joint ventures, wholly owned subsidiaries, or licensing agreements and the consistency in the application of the policies. The procedural aspects of the policy refer to the steps that have to be taken by a foreign investor to begin operations and to meet any requirements during its investment and the time it takes for all these procedures to be attended to. Once they make a decision to invest, they will want to start operations as soon as possible. By streamlining the approval process, Central Government approval is no longer required in India. However the similar amount of form filling required earlier must still be done. The more serious matter of continued bureaucratic veto power arises mainly from India's federal system. Each Indian state mimics the old Central Government apparatus of control although the licences required by the states tend to move towards upholding the decree of economic planners.

The legal aspects of policy refers to the tax and non-tax incentives provided to foreign investors by the Income Tax Act, the regulations regarding the formation of a company under the Companies Act, and the rules regarding the repatriation of profits and earnings. We wanted to see if these aspects of policy played any part in a firm's decision to invest.

Indian bureaucracy is also an important factor affecting foreign direct investment. A large number of bureaucratic hassles may deter foreign investors wishing to make investment across India. Bureaucracy involved the amount of red tape involved in getting approvals, the time taken for these approvals and the procedure that must be adhered to during the course of operations, that prevent the smooth operations of the project. We examined the following bypotheses:

H.1: Is the provision to hold majority foreign equity holding important to foreign investors?

H.2: Do investors experience delays in obtaining approvals? Why are these delays caused? Are there any bureaucratic hassles experienced during the course of negotiations?

Research Framework

The framework provides below a useful framework for analyzing the policy factors affecting foreign direct investment in India. The model suggests that foreign direct investment into India is influenced by various aspects of policy. In India's case, the Government has regulated the entry of foreign direct investment to the country through the post-Independence period via a highly selective industrial policy. This has tended to lower the magnitudes of potential inflows of foreign direct investment. On the other hand, outward foreign direct investments by Indian enterprises, that started to emerge during the 1970s though restricted, were encouraged by the Government. Because of this, India may have been a net exporter of foreign direct investment for a brief period during the late 1970s. This study looks at inward inflows of foreign direct investment only.

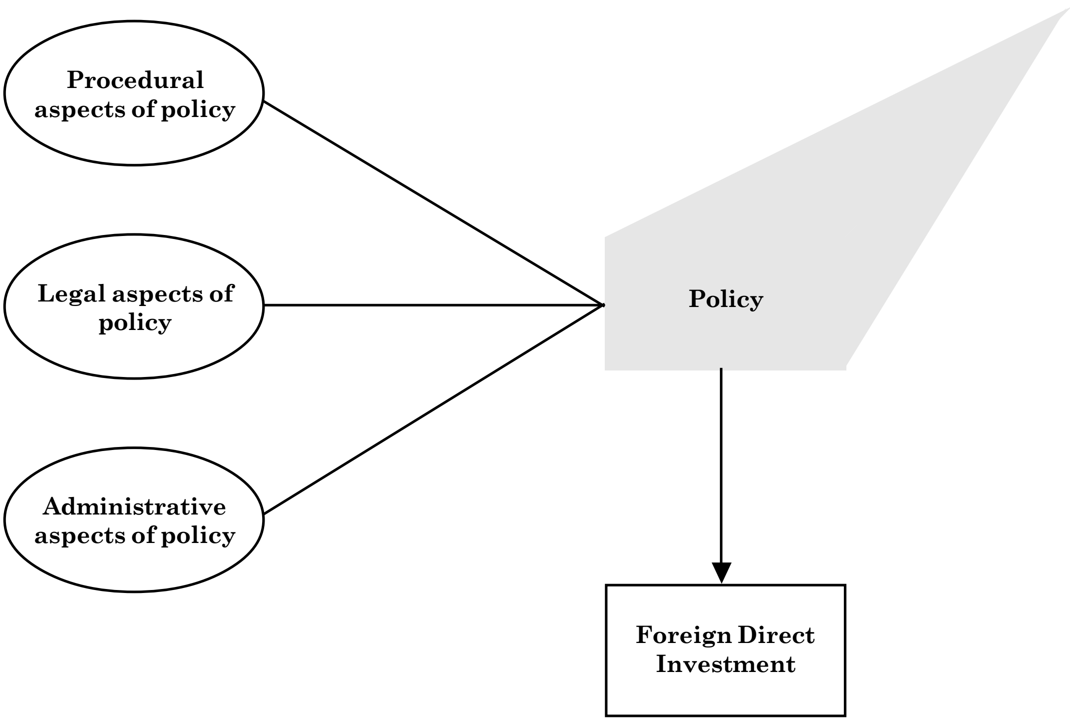

Figure 1 : Research Framework

Research Methodology

Detailed interviews were conducted on two groups: firms and experts (academics and government officials) to collect the data required for this study. Personal interviews were conducted with firms located in Singapore, whih have investments in India; the joint venture of these firms in India, and government officials and academics in Singapore and India. Information on investments by firms in Singapore and India was obtained from the publications of the Singapore Trade Development Board and the Singapore Indian Chamber of Commerce and Industry.

Research was carried out in two parts: preliminary study followed by final study. Preliminary study was done by telephone and was intended to obtain information from companies of their investments in India including: the nature of the investments of the firms, that had operations in India, to qualify the company as an appropriate subject and to ascertain which companies will be willing to participate in the detailed study at a later date. At the time of conducting the final study, a total of 20 companies in Singapore agreed to participate in our study. In addition, interviews were conducted with government officials and academics in Singapore and India. These interviews were intended to obtain a theoretical perspective on the liberalization efforts of the Government of India and the impact, which these efforts have had on foreign direct investment.

The interview questions were open-ended and were supplemented with appropriate probing questions to gain further insights into the issues and to explore issues that were seen to be important to the respondents. Apart from the questions in the interview questionnaire, questions were also asked to explore broader issues such as the nature of the company's investment in India, whether the company had any investments in any other part of the world or intended to invest in other parts of the world.

Findings

The major findings of our study on the issues identified above are as follows:

Industrial Policy

The findings of the effect of industrial policy on a firm's decision to invest in India are presented under two separate sections, policy and bureaucracy.

Policy

Our interview data reveal that economic reforms had always been on the government's agenda but were never pushed sufficiently. As stated by one expert, "India always had a positive attitude towards foreign direct investment right through the 1980s but never pursued it in a systematic manner until 1991". Various attempts to liberalize the economy had been made during the 1970s and the 1980s. To quote an expert on the description of the Indian economy: "For a long time, India was an open society but a relatively closed economy." The need for liberalization was brought about by external and internal circumstances and one expert felt that these circumstances explained the slow pace of reforms. The external circumstances may be explained by the collapse of the Soviet Union and the end of the Cold War, that was the political context in which India re-examined its relationship with the outside world and took the political decision to have economic reforms. These external circumstances coincided with the internal circumstances namely the balance of payment crisis and the structural adjustments which had to be taken under the directives of the World Bank and the International Monetary Fund. The need for liberalization had been thrust on the government rather than being a purposive step. Experts and companies share the view that the presence of a favorable policy towards foreign direct investment acts as a facilitator to foreign direct investment. The announcement of the liberalization policy of the government of India acted as a trigger to encourage many firms to consider investment into India. There were also many firms, which had always viewed India from the sidelines but could not invest in India because of the industrial policy of the Indian government. Of the 40 firms interviewed, 35 firms had considered investing in India only after 1991 when the economy was liberalized. If the policy is not favorable to foreign direct investment, whatever locational advantages are present, an investment cannot take place. The presence of a favorable policy enabled firms to invest in India and facilitated investment into India.

However, once there was an open door policy towards foreign direct investment, the policy which enabled foreign investors to hold more than 51% equity in a company was considered significant. Of the 40 companies interviewed, only 2 companies were willing to invest in India if the equity holding permitted was less than 50%. One company wanted 100% equity and was at the time of interview negotiating to convert its 99% equity participation in a power project to 100%.

The policy of the government may also have an indirect effect on a firm's decision to invest in that the change in policy in one sector may cause an increase in investment in another sector due to the increase in demand for the latter's products or services. One firm in the infrastructure industry commented that the demand for office space increased as the government announced policies, that encouraged firms to engaged in the IT industry.

All the companies interviewed, with the exception of one, indicated that the presence of tax and non-tax incentives did not affect their investment decision as any tax payable was included in the cost of production. They also felt that tax and non-tax incentives given were not important as these were usually matched by other countries wanting foreign direct investment. Of the companies interviewed, two had repatriated their earnings and had found no difficulty in doing so as long as the necessary procedure were followed when the money was invested in India. Companies that had still to repatriate their earnings stated that they did not think it would be a problem but should there be any, they would consider reinvesting their earnings for future expansion of their operations. The issue of repatriation only comes when the proper procedure had not been followed when the money was brought into India.

Bureaucracy

Our interview data reveal that bureaucracy and the procedural aspects of industrial policy were related. The procedural aspects of the industrial policy refer to the procedural requirements, that were needed to obtain requisite approvals and begin operations. Bureaucracy refers to the cause of delays in obtaining these approvals and beginning operations. There are two levels of Government in India, the policy level which is at the central/federal level and implementation which is at the state/provincial level. Policies are formulated by the central government but have to be implemented in the states as the foreign direct investment is going to take place in the state. The firms and experts interviewed felt that there was a difference in the formulation and implementation of policies at the centre and the state levels and this difference adversely affected a firm's foreign direct investment decision. Bureaucracy and the procedural aspects of the industrial policy are the main impediments to an investors' decision to invest in India. One company interviewed had divested its interest in a project as it found that the time taken to obtain the approval to commence operations was too long. The company had waited for two years but there was no progress in obtaining the requisite initial approvals.

At the centre/federal level, approvals are given by the Foreign Investment Promotion Board or the newly set up fast track approval procedure of the Foreign Investment Implementation Authority. All the companies interviewed agreed that they had not experienced any problem obtaining approvals at the centre level, the only issue was one of pace, that is, whether the approval is obtained in one day or three months. According to the New Economic Policy 1999, the approval has to be granted within three months. However, once this approval is obtained, the investor has to get approvals at the state level. As stated by all the respondents the single-window clearance as is stated by the new economic policy is "on paper only and not in practice". In practice, there were a large number of clearances that an investor had to obtain. An example is the case of an investor in the hotel industry who claimed that he needed to obtain 80 approvals at the state level. There is a procedure to obtain these approvals in that following the list of approvals required, if one approval is not obtained, the investor cannot proceed to obtain the next. This is due to the difference in formulation and implementation at the state and centre levels. The idea of liberalization shared by the central government has not filtered to the states. The respondents felt that, at the state level, the higher end officials and politicians might be pro-liberalization but at the lower end of the bureaucratic hierarchy, the officers were not and they have tremendous opportunity to sabotage any procedure as the forms have to pass through them first. The respondents felt that these officials were primarily reticent about liberalization because all they had is the power of patronage and they would lose this if they had a one-stop clearance system. As explained by one expert, "there is a tremendous amount of reluctance from this group of people. They are also the ones who follow the laws in such a way that crossing the T's and dotting the I's can take forever; files can move only because some extra incentives are given, that are not really written down". As a result, a great deal of bottlenecks are created at the state level.

The experts interviewed felt that an understanding of the slow pace of reforms at the state level might enable the firms to understand why it was difficult to get approvals at the state and thus they might not be deterred from investing in India. First, the state political leaders have short time horizons. Several state governments are coalitions of diverse political parties. Chief Ministers [the political heads of state governments in power] are often opposed by factions in their own parties. Their precarious political situation forces state leaders to think of the short term effects of policies. Secondly, many organizational interests opposed to one or the other aspect of economic reforms have considerable political clout at the state level. Through public protests, civil disobedience, strikes, appeals to the media and public interest litigations, these organized groups have been able to halt government initiated programmes. As stated by one expert, "It is politically easier to liberalize the trade regime, simplify investment rules, devalue the currency, and lift restrictions on the capital markets - all decisions made by the central government, than it is to revise labor laws, reduce subsidies, permit bankrupt firms to close, and privatize state-run enterprises, decisions that have larger public impact and require actions by the states." Thirdly, the state and local officials, bureaucrats, and police officers are reluctant to give up the patronage and the rents that are acquired through the existing regulatory system. Patronage in public sector enterprises remains an important source of jobs. Officials gain from the maintenance of regulations that require the inspection of places of business and the renewal of licences.

The firms interviewed had varying experiences in obtaining approvals at the state and their approvals had taken anywhere between nine months and two years before operations could begin. There was a difference in the time of getting approvals and the number of approvals depended on the sector in which the investment was made. Firms with investments in the power sector, found the most difficulty in getting approvals. Of the firms interviewed, four were involved in power projects in India. Two were based in Malaysia and two were based in Singapore. Two of these firms had not obtained approvals for their projects even after waiting for two years.

One expert stressed that it was important that firms should not be too hasty in blaming the bureaucracy for every delay that is occasioned but rather to look at the underlying reason for the delay in obtaining the approval. Although there are certain reasons for state level bureaucracy as explained above, in many cases there were other problems present that brought about the delays. The following examples were cited by the expert to illustrate this point. The delay in the power sector projects was because firms investing in the power sector wanted fuel supply contracts, that restricted them from risks of fuel supply interruption by providing for sufficient compensation in the event of non-performance by either the public sector coal supplier or by the railways, that have to transport coal to the power plant. Such contracts had never been signed for coal suppliers to public sector projects and there was reluctance on the part of public sector suppliers to accept new obligations for private sector projects. Private sector telecommunications projects could not achieve financial closure because lenders insisted that in the event of debt service default by original licencee, the telecom licence should be assignable at the option of the lenders to the new operator. The terms of the licence under Indian law did not provide for easy assignability and new provisions had to be devised to meet these requirements. This was an important source of delay in implementation.

All experts attributed these bureaucratic hassles and delays due to India having followed a socialist economic model which had resulted in it having pursued a closed door policy for 40 years. This had impeded economic reforms to a considerable degree and developed the system to an extent that it could not be reversed. The bureaucrats had formed a socialist mindset that has been very difficult to change as a result of having inherited lot of etiquettes from the colonial times, and vested interests. The experts however felt that the mindset of investors had to change as well. Investors especially from Singapore were used to having matters handled in an official manner, quickly and efficiently so that they cannot understand any delay that they may come across in India. There were certain cultural and historical traits present in India that firms in Singapore and Malaysia did not understand but which they should take steps to if they want to invest into India successfully. For four decades India's state governments had relied upon the central government to set the overall strategy for the development of the country, and to determine the flow of resources by sector and location. Thus were not familiar with the idea of making decisions themselves and hence may not make a decision because of the fear of making a wrong one. As explained by one expert, "the reform process in India simply hasn't been as fast as Singaporeans are used to, but I think Singapore is beginning to understand that through the political process, reforms are slowly being accepted with grassroots consensus, that is a great achievement."

The presence of the bureaucrats on the governing platform of India should be looked at from more pragmatic perspective. As explained by one expert, one of the greatest assets of the Indian democratic system is the steel frame of its bureaucracy, that has kept the country united inspite of political chaos, cession movements and socio-religious conflicts across the country. It did play a beneficial role by providing for stability, and the institutional mechanism so that India did not start off bankrupt as far as the governance or institutions were concerned. It is the way the bureaucracy has developed over the years because of the power of patronage that they possess, and corruption present in the system. It has been very counterproductive as far as development of the country is concerned.

Conclusions and International Business

The economic landscape in India has substantially changed since 1991. The rate of inflation for consumer goods price was brought down to 10% in 1995–1996. Inflation was declined throughout most of 1997, with the deceleration most marked in wholesale prices, where annual inflation remained in the 3–4% range in the five months from July 1998 and consumer prices was 6%. The rate of growth of gross domestic product increased to over 5% in 1994–1995 as compared to less than 1% in 1991. It was expected gradually to increase thereafter to reach 5.9% in 2000. Growth rate, which was 0% in 1991–1992 and 3% in 1993–1994, is expected to average 5.5% over the next 5 years. The foreign exchange reserves of the country stood at a respectable US $42 billion in 2000, compared to US $8 billion in 1991-1992 or even $19 billion at the end of August 1994.

There is ample evidence to show that India will not backtrack on its economic reforms already in full swing (Joshi, Zutshi and Ahmed,1999). There are various reasons for this: there has been consensus on its economic reforms taken to date. This is evident from the fact that regardless of the frequent changes in Government during the previous years, the reforms have continued. As international companies throughout the world have become more competitive and the products more identical to each other thanks to the emergence of more and more global brands investors need to look for virgin pastures to capture markets instead of established ones in order to create a niche and gain a foothold in their market. India is relatively an untapped market of one billion consumers and 200 million strong middle class, that has a great potential to attract FDI. Also, India has a very large diaspora of nearly 20 million Non–Resident Indians living across the world. Millions of them are world class entrepreneurs and professionals whose contribution to India has been nominal in the past. India recognizes the need for an open market attitude to tap its own talent. NRIs possess money, technology, marketing know-how, financial expertise, a good understanding of local customs and experience obtained from being abroad, all of which could emerge as a powerful tool in reshaping India's economy in the third millenium. Many firms interviewed stated that they viewed India favorably as a long term investment destination.

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