# Uncertainty and FDI in India: A Tripartite of Expectation, Complexity and Inexplicability

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*Abstract*: **A policy creates an effective and attractive environment for investment and increases the confidence in investors to invest their money in the market for gaiting the higher profit. The policy which attracts the foreign investors is craft of central government of the host country. The objective of present research paper is to find the relationship between economic policy uncertainty and FDI inflows into India and evaluate different times' different political ideologies' central government in India. The period of study is taken from April 2005 to December 2022. Explanatory as well as exploratory methods are use for data analysis. In the result it is found that as the time passes and policy become the strong and uncertainty reduced and it attracts FDI. As central government's economic policy is as becoming the liberal and investment friendly, it is reducing the uncertainty in the Indian economy. Due to that the foreign investor are showing their interest to invest their capital and it is playing major role to boost the Indian economy.**

*Keywords*: **Policy Uncertainty, EPU, Investment, Policy, Macroeconomy, Foreign Direct Investment, FDI.**

## INTRODUCTION:

While foreign direct investment (FDI) is known to be the most stable type of international capital inflow, it can be particularly susceptible to greater uncertainty due to its high fixed costs and the uncertainty of domestic politics in a host country flows, with the effect being greater in countries with low financial development (Choi, S., Furceri, D., & Yoon, C., (2021). Countries with high levels of political-economic uncertainty In addition, although countries with a high level of financial market development attract more FDI inflows, domestic uncertainty, even in the presence of more developed financial markets, remains a barrier. Hence discourages FDI inflows (Nguyen, C.P. & Lee, G.S., 2021). Using the timing of national elections as an indicator of political uncertainty, Chen, K., et al. (2019) found that FDI declines significantly in election years when political uncertainty increases. The negative impact of political uncertainty on FDI depends on the degree of democratization and also on the political system. In democracies and countries with a president elected by the legislature, the decline in FDI is more pronounced in election years. Rivoli, P. and Salorio, E. (1996) point out that in uncertain environments, the advantages of ownership and internalization may be more negatively associated with FDI than positively. This reversal of existing theory is because ownership advantages often delay FDI, while internalization advantages often serve to make it less reversible. When FDI becomes more delayed or less reversible, it is less likely to happen any time soon. The relationship between legal system uncertainty and FDI attractiveness is curvilinear in nature, such that FDI attractiveness decreases with legal system uncertainty up to a critical point, but then increases beyond this point; and that the relationship between legal system uncertainty and FDI attractiveness is moderated by government intervention in the host country's economy, such that the strength of this relationship is greater when government intervention is high than when it is low. (White III, et al., 2015).

## REVIEW LITERATURE

Several models in the financial literature argue that economic agents have a preference for the rapid resolution of uncertainty and that economic uncertainty has an impact on the stock market (Dzilinski, M., 2012). On the other hand, studies in economic psychology consistently suggest that the typical response to uncertainty is to increase information seeking (Lemieux & Peterson, 2011). The index is higher in recessions, elections, monetary policy surprises and some major events; increases faster than it decreases and is driven by both internal and external factors (Moore, A., 2017). Baker, S.R., et. al (2020) in their explanatory exercise that the COVID-19 disaster will cause a large contraction in output, more than half of which is due to COVID-induced economic uncertainty. Sorik, P., & Lolik, I. (2017) find that its effect on industrial production is stronger at the beginning of the crisis. On the other hand, the effect of fiscal uncertainty shows exactly opposite trends. It tends to strengthen with an intensification of economic activity, which partially offsets the potential use of fiscal expansion as an anti-crisis tool. Greater uncertainty in the US is associated with less political influence not only at the national level, but also in Canada (Estwit, K.A., et al. (2013).

## OBJECTIVES

The objective of the present research paper is to access the impact of economic uncertainty on Foreign Direct Investment inflow into India during different parties' role as centre government of India.

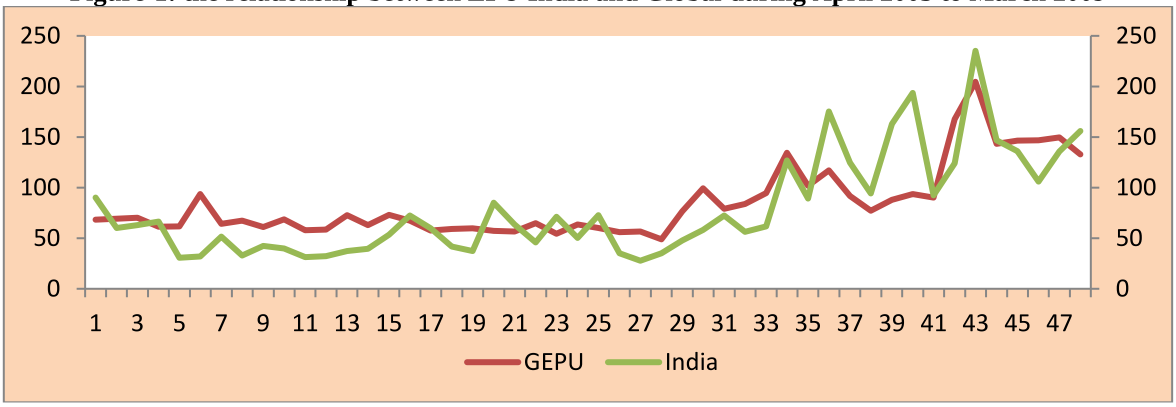
## METHODOLOGY

The used data for analysis is secondary collected from department of industrial policy and promotions and economic uncertainty index by https://www.policyuncertainty.com. The period of study is taken from April 2005 to December 2022. Explanatory as well as exploratory methods are use for data analysis. The all period is divided into four parts based on different political ideologies'

various period of central government in India. First part is from April 2005 to March 2009, second is from April 2009 to March 2014, third is from April 2014 to March 2019 and forth part is from April 2014 to December 2022.
The deflators of policy uncertainty and FDI are used for graphical representation and understanding. Uncertainty and risk are one of the important determinants of investment. The openness of a macroeconomy divided the investment in term of domestic foreign. Broadly, uncertainty can be measured in basis of perception in the economy and economic stability indicator. The perception of uncertainty anchors the investors. EPU is perception based measurement of uncertainty. It is carefully calculated by experts by doing content analysis of popular news papers of different nations. As uncertainty increases the repetition of uncertainty related word also increases. Therefore, number of words' repetitions is a way to develop uncertainty related index.

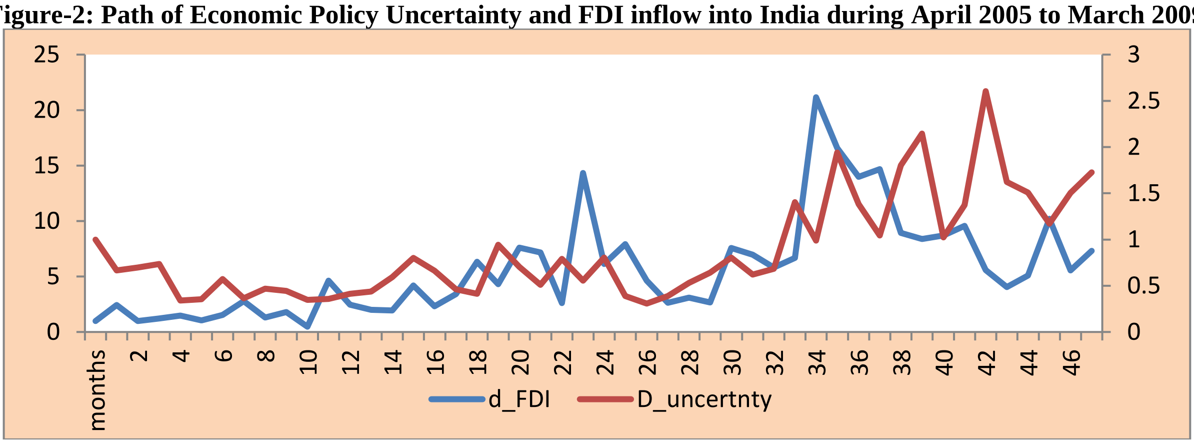
**ANALYSIS AND RESULTS**
Investors are rational economic agents and Homo-Economicus. The behaviour and pattern of FDI in India can be explained in the trinity of word-rational expectation, complexity and inexplicability. To simplify the analysis, we divide entire period of concern on the basis of some political and economic characteristics of that regime of Indian governance of FDI. First, we look the pattern for the global uncertainty, second we try to find out the pattern of uncertainty in India with inward FDI. The figure-1 and 2 are complementary composite for reading the pattern and analysis of FDI in India. Similarly, figure-2 and 4, figure-5 and 6, and figure-7 and 8 are complementary sub-set of each other. The first outcome is that high global uncertainty is a bit of positively correlated with the FDI in India. For instance ultra easy global monetary policy in advanced economies induced the FDI with Indian definition of FDI after the global financial crisis. Second the uncertainty in India is phase-wise positively and negatively correlated with FDI, the showed the complexity of FDI pattern. The positive correlation of uncertainty in India and FDI in India is a sign of inexplicability.

**Figure-1: the relationship between EPU India and Global during April 2005 to March 2009**



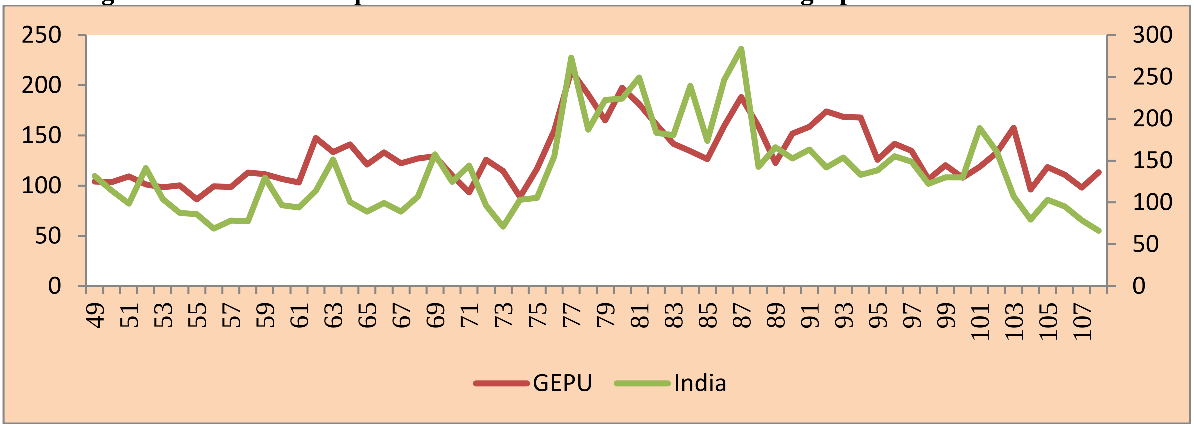

Sources: Economics Policy Uncertainty Index

**Figure-2: Path of Economic Policy Uncertainty and FDI inflow into India during April 2005 to March 2009**



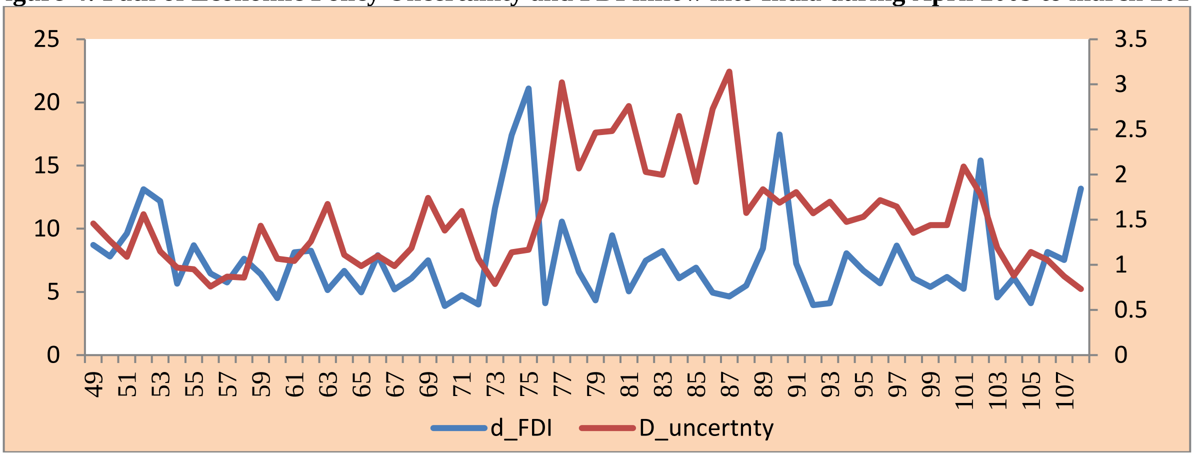

Sources: FDI Factsheet and Economics Policy Uncertainty Index

**Figure-3: the relationship between EPU India and Global during April 2009 to March 2014**



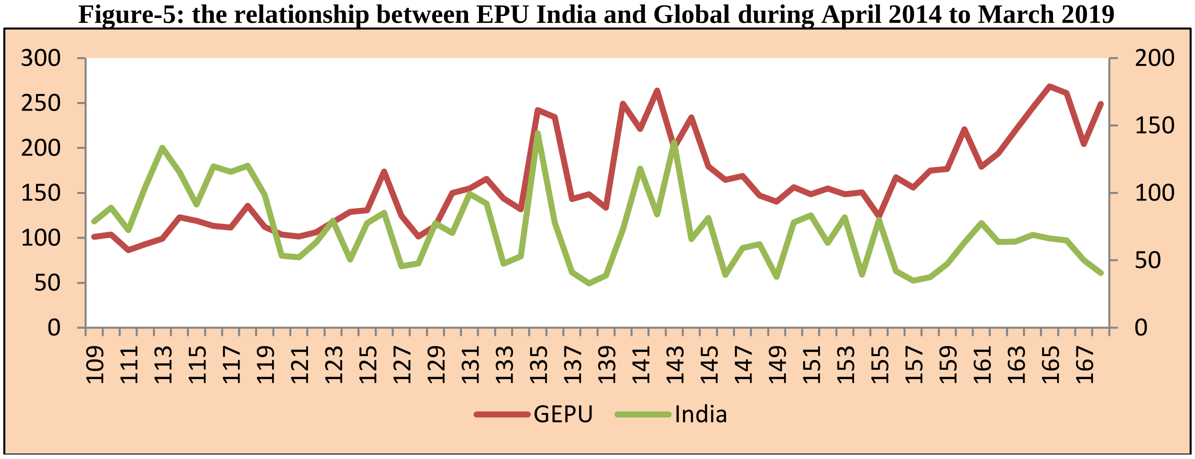

Sources: Economics Policy Uncertainty Index

**Figure-4: Path of Economic Policy Uncertainty and FDI inflow into India during April 2009 to march 2014**



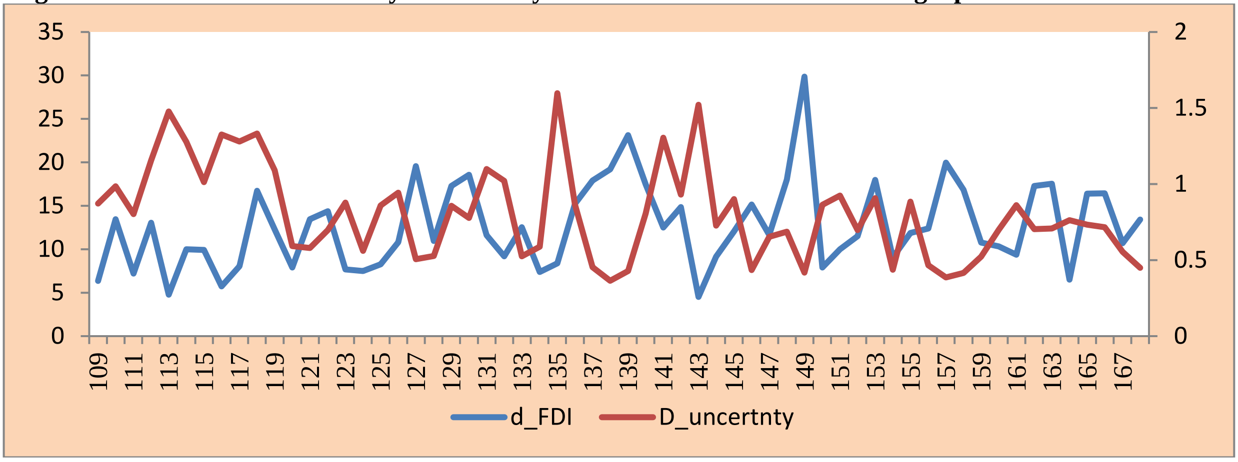

Sources: FDI Factsheet and Economics Policy Uncertainty Index

**Figure-5: the relationship between EPU India and Global during April 2014 to March 2019**



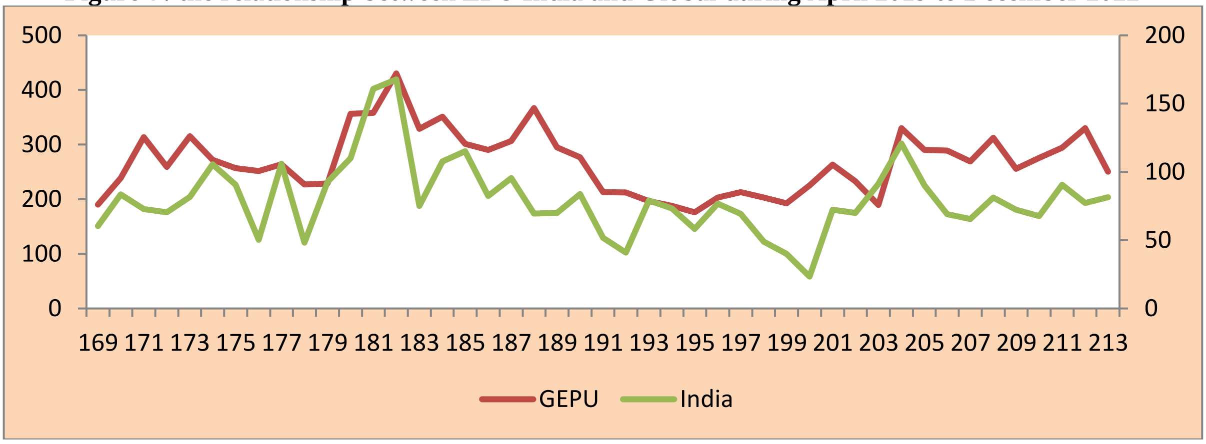

Sources: Economics Policy Uncertainty Index

**Figure-6: Path of Economic Policy Uncertainty and FDI inflow into India during April 2014 to march 2019**



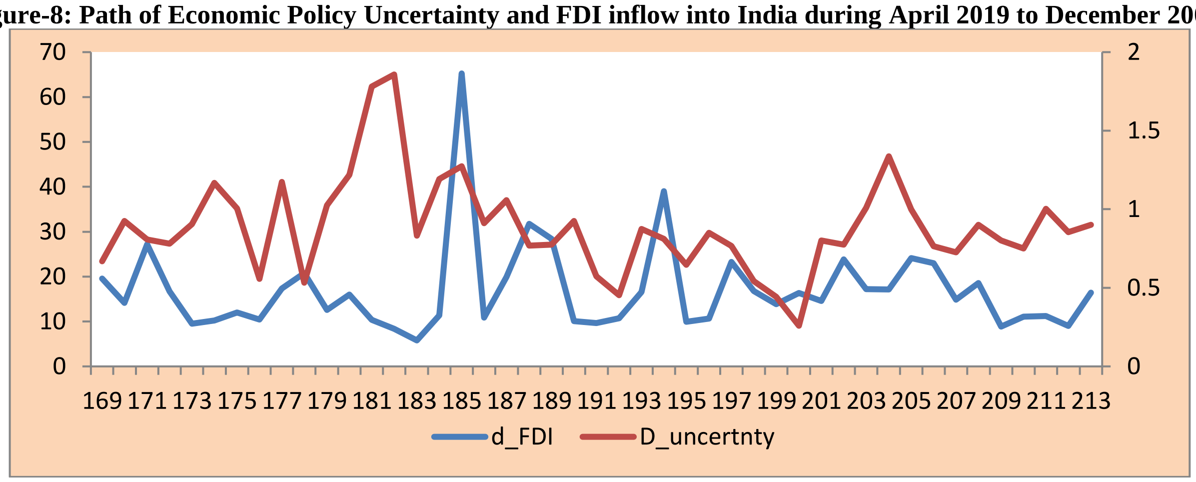

Sources: FDI Factsheet and Economics Policy Uncertainty Index

**Figure-7: the relationship between EPU India and Global during April 2019 to December 2022**




Sources: Economics Policy Uncertainty Index

**Figure-8: Path of Economic Policy Uncertainty and FDI inflow into India during April 2019 to December 20022**




Sources: FDI Factsheet and Economics Policy Uncertainty Index

The figures 1,3,5,7 are presenting the relationship during the different period between global EPU and India. There are same months during which the GEPU (Global economic policy uncertainty) and IEPU (economic policy uncertainty in India) are walking together till march 2015, but that the GEPU walks upward and IEPU goes down with some fluctuations. In the figure-5, IEPU makes much difference with GEPU, and also make the stability in the Indian economy.

The figures-2,4,6,8 are presenting the relationship between FDI inflow into India and IEPU. In all four figures this relationship is negative and walks according to EPU definition. But some periods are there, where EPU and FDI inflows are same in directions and make the positions relationship. The periods are June-July 2005, August-September 2013, February-April 2015, December 2015-March 2016, November 2017 – February 2018, August- October 2021, there are same periods of tripartite of expectation during these period when explanation is not clear in itself.

**Table-1: Cause and impact of policy uncertainty of India and Global on FDI inflow into India**

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Regression with Newey-West standard errors          Number of obs   =       213
maximum lag: 0                                      F(  2,    210)  =      6.00
                                                    Prob > F        =    0.0029
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| FDI_inflow | Coef. | Newey-West Std. Err. | t | P>\|t\| | [95% Conf. | Interval] |
|---|---|---|---|---|---|---|
| EPU_India | -5.933116 | 1.973352 | -3.01 | 0.003 | -9.823235 | -2.042998 |
| EPU_Global | -1.864536 | 1.40906 | -1.32 | 0.187 | -4.642251 | .9131782 |
| _cons | 3687.673 | 341.3843 | 10.80 | 0.000 | 3014.694 | 4360.652 |

Sources: FDI Factsheet and Economics Policy Uncertainty Index

The table-1 shows the regression of FDI inflow into India for economic policy uncertainty of India and global which shows negative. The model is statistically significant with 1 percent of level of significance. The relationship between EPU India and Global with FDI Inflow in to India is negative and EPU India is significantly impacting on FDI with boom of 593 percent. But EPU global is not statistically impacting significant on FDI India. Foreign direct investment (FDI) is a sort of international business in which an investor from one nation has long-term ownership in and substantial control over a company from another one (Blonigen, 2005). The significance of economic policy uncertainty grew with the occurrence of multiple economic and financial crises, which led to a decline in FDI inflows for host nations (Albulescu & Ionescu, 2018). The concentration of global economic uncertainty as a factor of FDI is superior for developing economies than for developed ones for gross investment flow (Hlaing & Kakinaka, 2019). The strong economic governance institutions on the continent may be responsible for the persistently increasing FDI inflows to India compare to other regions of the world.

## CONCLUSION AND SUGGESTIONS:

The FDI in India is mixedly determined by rational expectation. The political governance and global scenario determined at a largely. It is not a stable political environment only but many factors work together to explain the pattern of foreign direct investment. The FDI is political, economic, geographical and environmental and social phenomenon. Neither alone political nor alone economic factors explain it.

The different political ideology creates a different policies for investors sometimes its show leftist ideological policies and some sometimes it shows rightist ideology. But ultimate it is seen that as the central government came in majority the investment policies become the liberal and friendly to the foreign investors to invest their capital in Indian economy. After 2014, majority government sets up the high order norms for investment and provide the confidence to the investors local as well as international.

The stability of the India's political environment and consistency in government regulations favouring foreign investors are economic consequences of the study. Therefore, the policymakers in high income economies should recommend that governments and relevant authorities stabilize their laws and political environment and make a favourable economic environment for international investors that encourage them to enhance their investment in Indian economy. Strict laws and a difficult political and economic environment may discourage foreign investors, which ultimately decline their investment in Indian economy of high-income groups. The implications also contain stabilizing the exchange-rate, and inflation-rate to attract more foreign investment into India. In totting up, governments must give confidence trade frankness and real growth in the world's higher-income economies to increase foreign direct investments in India.

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