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JGBC JOURNAL FOR GLOBAL BUSINESS AND COMMUNITY
ISSN: 1934-4244

American-Indo Trade: An Economic Opportunity

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Abstract

The U.S. and India have had a long and successful economic relationship. After a period of economic liberalization, India is ripe for rapid economic growth. American Foreign Direct Investment is the catalyst for economic expansion in every sector of the Indian economy. This article examines how American investment, trade, and aide areunlocking India's untapped economic potential.

India has seen a major influx of FDI flow from the U.S. over the last 25 years. To fully understand the effect of FDI, one must analyze the allocation of these investments according to industrial sector. India today has one of the largest and fastest growing consumer bases in the world. With a population of over 1.2 billion and almost 1.8 trillion in GDP, India has become a major emerging market, with major financial and industrial organizations taking notice.

American multinational corporations and the financial institution are investing large amounts of capital into the Indian economy. The financial sector sees names like Goldman Sachs and J.P. Morgan investing billions into green energy and large-scale industrial projects. Companies like GE and Caterpillar have also begun major construction projects in India. The most well-known source of foreign capital in India has been information and technology companies. American FDI and technical innovation are reshaping not only India's economy, but also India as a whole.

Market Liberalization in India

The Indian market has not always been open to foreign investment. After independence and up through the early 1990s, India chose bureaucratic socialism as its form of economic policy. This choice led to tight governmental oversight and stifled economic prospects. Eventually, the country began facing major economic and fiscal problems, which culminated in 1991 with the Indian Economic Crisis of 1991. During this time, the situation became so dire that the Indian government was forced to airlift 67 tons of gold to secure loans from the International Monetary Fund. This brush with economic collapse led to the welcoming of decentralization, as well as major reforms toward liberalization. First, the country opened up for international trade and foreign direct investment. Many state run industries were regulated, inflation controls were initiated, and some privatization occurred within service sectors. This loosening of economic markets has contributed to rapid GDP growth during recent decades.

This economic liberalization led to the integration of India into the global economic community. In 1995, India joined the World Trade Organization and then became a member of the United Nations. Today, the Indian stock market trades in global commodities and is one of the largest exchanges. By opening the Indian economy, India’s policy makers have accepted the advantage of capitalism and embraced the country’s place as a global player.

Multinational investment in India comes from financial institutions and corporate enterprises. The era of outsourcing in the early 2000’s had great effect on the flow of jobs and FDI. The telecom’s industry saw multifold growth in the number of companies and jobs available for Indians. Major cities became tech hubs and started attracting business. Global technology companies that transfer jobs to India simply have to allocate resources to create the infrastructure.

U.S. banks have invested over $2 billion in India since 2006. They continued to invest during the U.S economic crisis that began in 2008, showing how much potential these private financial institutions saw in India as an emerging country. Marquee investors like Goldman Sachs agreed to acquire a majority stake in India’s Renew Wind Power for $200 million, thus extending the U.S bank’s investments even further into India. Multinational corporations such as Microsoft, Google, General Electric, and Caterpillar also play a large role in FDI.

Google Chairman Eric Schmidt has launched an ambitious program for technology entrepreneurs in India that will invest some $10 million to nurture 10,000 new businesses within the next five years. Also, GE is expanding its presence in India by partnering with one of the country’s fastest growing clean energy developers. GE Energy Financial Services and Indian based Greenko Group plc. have agreed to invest $50 million and $65 million respectively into a new venture to develop wind energy projects across India. Moreover, Caterpillar Inc. invested $210 million into India as they look to improve infrastructure development activities and capitalize on an expected increase in road construction. The company will invest an additional $150 million to build a new facility that will produce its Perkins branded 4000 Series engines and $62 million in its existing off-highway truck manufacturing facility in Chennai. This new investment is alongside a $108 million investment to expand truck capacity in Chennai. Caterpillar has a total of three manufacturing facilities, one logistics services base, and one research and development center in India.

The U.S. government has provided over $4.2 billion in aid to India as well. This aid has been direct liquid cash infusions to serve as an investment into key sectors. In 2011, America's goods and services trade with India totaled $86 billion; thus, India became the United States' 17th largest goods export market, 13th largest supplier of goods imports, and 7th largest supplier of agricultural imports. Consequently, U.S. FDI in India and India's FDI in the U.S. have both increased significantly since 2009.

U.S goods and services ran a total of $20 billion in trade deficit with India. Goods exports totaled $21.6 billion while goods imports totaled $36.2 billion, making the U.S goods trade deficit with India $14.5 billion. Exports and imports, or trade in services, totaled $28 billion. Service exports were $11.6 billion and service imports were $16.9 billion, creating a $5.3 billion deficit.

The top U.S. exports to India were precious stones at $4.6 billion, machinery at $2.9 billion, mineral fuel at $1.8 billion, electrical machinery at $1.5 billion, and fertilizers at $1.2 billion. American exports of agricultural products to India totaled $723 million. These agricultural exports are comprised of leading categories including: tree nuts worth $308 million, fresh fruit at $100 million, and cotton at $93 million. American goods exports to India were $21.6 billion in 2011, up $2.4 billion (12.4%) from 2010 and up a remarkable 491% since 2000.

The top five categories of goods the U.S. imported from India in 2011 were precious stones at $8.0 billion, pharmaceutical products at $3.2 billion, mineral fuels at $3.2 billion, organic chemicals at $2.0 billion, and woven apparel at $1.9 billion. The leading categories of agricultural imports include: tree nuts at $319 million, spices at $221 million, essential oils at $139 million, rice at $124 million, and vegetable oils at $113 million. These imports totaled $36.2 billion, which is $6.6 billion (22.5%) more than in 2010, and 238% more than in 2000.

In 2010, America's FDI in India amounted to $27.1 billion, a 30% increase from 2009. The direct investment into India is led by the following sectors: information, professional, scientific, technical services, and manufacturing. India's FDI in the U.S. was $3.3 billion in 2010, a 40.8% increase from 2009. India's direct investment is focused on the professional, scientific, and technical services sector. In 2009, the sales of services in India by American owned affiliates were $13.1 billion in 2009, and sales of services in the U.S. by India-owned firms were $7.2 billion.

The development of a nation's infrastructure and economy take time. As India becomes a more popular destination for FDI and as its economy matures, it shall develop a more reliable infrastructure. Today, many firms are unwilling to invest in India due to this lack of infrastructure. Walmart is one example of a company that had invested in India but eventually withdrew from the country because of a lack of infrastructure. Infrastructure refers to the roads, the communication, the utilities, and even the government's regulations.

Corruption is also a major problem prevalent in India today. This acts as a direct impediment to the flow of foreign direct investment since it creates a sense of weakness and fragility. India is ranked by the Transparency International organization as the 94th most corrupt nation in the world. Thus investors see certain investment opportunities in India as risky.

There are also factors that work in India's favor. For instance, India has one of the world's largest railroad networks. Its railroad sector employs over 1.3 million people and spans the length and breadth of the subcontinent. The entire railway system stretches for over 41,000 miles. It transports everything from goods and people, to livestock and resources.

India is also recognized as a stable political and social environment. This fosters confidence in firms about the nation's ability to offer security and safety for their investments. The rule of law in India protects intellectual property and therefore recognizes the patents and privacy rights of individuals and their companies. This is in stark contrast to the Chinese government and their willingness to not only breach contract, but break laws as well. By creating an environment of openness and safety, India fosters goodwill and attracts further foreign direct investment.

India is also home to the world's second largest English-speaking population, second only to the U.S. Moreover, English is the default language of business in India. Any group from the U.S. or Europe would see that a familiarity in language with another nation is a major advantage.

Fortunately, the issues India faces as a recipient of FDI can be fixed. Creating a stricter set of internal affairs guidelines could significantly reduce corruption. By investing in its electrical grid, India can modernize faster. Instituting more stringent security regarding infrastructure would alleviate any fears foreigners may have regarding assets in this country. Furthermore, the creation of a wider system of transport for goods could link the nation's best talent and materials.

Starting in 1947, India became a free and sovereign nation. They chose socialism as their economic policy. This choice led to major economic problems in the long term that culminated in 1991 with a near economic collapse. The near collapse forced India to embrace a period of rapid reform. These reforms then opened markets and liberalized the government regulations constraining the private sector. India's economic liberalization opened its markets to global competition and investment. Over the last 20 years, the world has seen India emerge as a major economic and geo-political player. The nation's march towards modernization has made India a prime target for FDI. Other countries and corporations see India's outlooks as positive and hope to capitalize by investing in new infrastructure projects and major contracts. India has benefitted as well through its exporting of agricultural goods and produce.

There are many issues and hurdles the nation still faces, but a clear and coordinated effort can rectify them. In the coming years, India will continue to be one of the world's most popular and productive destinations for foreign direct investment.

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