

India's FDI palace of illusion

Record inflows mask problems of outflows and external claims

India mostly measures success in the foreign direct investment (FDI) arena by a single number. How much capital (money) came in during a year. When FDI inflows rise, the credit is instantly given to the reforms, and other policy measures. When they fall, global uncertainty and external factors are blamed, further liberalisation is promised, followed by additional "Ease-of-Doing-Business" steps. States compete to host investors' summits, incentives multiply, and the country's rankings improve. Over the past two-three decades, wooing FDI has quietly become an objective rather than an instrument. Hence, there is little systematic assessment of the overall economic impact.

In the recent past, the phenomenon of high gross inflows, coupled with large repatriations or outflows, is interpreted by the policy-makers as evidence that India not only attracts foreign capital but delivers strong returns. Foreigners bring in money to make money, a part of which they take out. This enhances India's reputation as a reliable investment destination. However, as the inflows come under serious pressures, due to stronger outflows, even resulting in net outflows, there is some thinking and introspection within the official circles.

According to the Reserve Bank of India (RBI) data, net FDI inflows fell sharply from \$44 billion in 2020-21 to less than \$1 billion in 2024-25, with preliminary estimates placing them at \$353 million, as reported under the balance of payments, which net inward and outward direct investment. The upward revision was mainly due to the revised estimates of reinvested earnings, which are from the profits earned by the foreign firms from their Indian operations. The figures in the four months (September-December 2025) remain negative.

Indeed, net FDI has turned negative, not merely because inflows slowed significantly, but larger amounts flowed out due to repatriations by the foreigners, sale of a part of their stakes, along with the rise in outward investments by the Indian firms. Even without considering the outward flows, net FDI fell in the recent past. During the four years from 2021-22 to 2024-25, gross FDI inflows were \$308 billion. Over the same period, repatriations, dividends, and royalty payments to the foreign promoters and shareholders came to \$296 billion (repatriations — \$154 billion, dividends — \$103 billion, and royalties — \$39 billion).

This left a mere balance of \$12 billion over the four years. This is after \$3 billion royalties are kept out of the calculations. In other words,



nearly 96 cents out of every dollar that came in went out via outward payments that were linked to the incoming FDI. If outward investments by Indian firms, which were \$75 billion, are added, the difference between what came in, and what went out is a huge negative \$63 billion during the same period. If one excludes reinvested earnings, which represent retained profits rather than an inflow of fresh capital, the picture becomes stark. The figure for gross inflows will be down to \$227 billion, and the net FDI deficit will be \$69 billion.

When India opened its economy in 1991, FDI was welcomed for clear reasons. The objective was to acquire technology, promote exports, and strengthen the domestic industry. In particular, the Industrial Policy (1991) emphasised building the country's capacity to earn foreign exchange. Entry was selective and linked, at least in intent, to capability creation in what were termed as high priority industries. Higher dividend payments to the foreign parents, due to an increase in their respective stakes up to 51 per cent that was allowed in most sectors, were to be balanced by companies' exports.

Automatic approval was extended to technology agreements related to high-priority

industries. Thus, liberalisation was directly linked to technology, exports, and conservation of foreign exchange. Even so, a tension remained between reforms and external sustainability. Gradually, the emphasis shifted. Restrictions were eased across sectors, performance requirements disappeared even before those were outlawed under WTO, and the distinction between types of investments faded. The concept of dividend balancing was removed, and royalty payments were liberalised. Instead of asking what the investments would do for the economy, the policy asked how easily it could enter.

By the early 2010s, foreign investment became a means to finance the current account deficits rather than to achieve the well-documented benefits that were reiterated by the Industrial Policy of 1991. The fact remains that capital inflows bring money today but create claims on the domestic incomes tomorrow.

These appear as dividends, royalties, technical fees, and capital repatriations to the foreign parents. As foreign firms mature, these payments rise. In addition, there is invariably the important issue related to technology transfers.

A Discussion Paper (2017) suggested that a

review of the FDI policy was needed to "ensure that it (FDI) facilitates greater technology transfer, leverages strategic linkages, and innovation." Instead of issuing a new comprehensive industrial policy, the Government opted for a piecemeal approach. A decade earlier in 2008, an Expert Group under the National Manufacturing Competitiveness Council described how the liberal FDI policy had hurt Indian manufacturing. It observed, "Technology transfer is considered to be one of the most important benefits of permitting FDI.... In India, however, in attracting FDI, the emphasis appears to be substantially on the amount of FDI flows."

Purchase of technology is costly, and in view of the liberal Indian policies, foreigners are reluctant to part with it. Even when the Indians are willing to buy it, there are apprehensions or unwillingness. In the pre-reforms days, the foreigners were skeptical about restrictions, and the policy environment. In the post-reforms period, they were eager to earn regular royalties, fees, and other compensations, rather than part with proprietary technology. This explains why the Group wanted a high-level technical committee to review the FDI policy.

Hence, the FDI arithmetic reveals only a part of the whole story. The deeper question is whether this investment trajectory was anticipated but not acted upon sufficiently. When one understands the overall architecture behind the FDI patterns, it becomes clear that the emerging imbalance is not the result of a single policy error or a sudden loss of investor confidence. There are contributory factors to the burgeoning outflows, and the trends are embedded in FDI's nature, India's liberalisation curve, and evolving character of global capital.

Understanding these shifts is essential if policy recalibration is to be deliberate rather than reactive and enthusiastic. A deep analysis can ensure that openness strengthens domestic capability rather than gradually expanding the external claims. We will examine these and other issues in the second part of FDI's magic show. Watch this space tomorrow for more insights, some surprises, and a few shocks.