

Foreign Capital, Local Growth: Rethinking FDI's Role in India's Entrepreneurial Landscape

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Abstract

In emerging economies, Foreign Direct Investment (FDI) has become the engine of growth. India in particular has been the major country to attract global capital flows over the last three decades. The aim of this paper is to investigate the impact of foreign capital investment on domestic investment and entrepreneurship in India, focusing both on the opportunities and challenges provided by foreign capital inflows. FDI will spur domestic economic development by the process of accelerating capital formation, introducing new technologies in managerial practices, creating new opportunities in the market for the domestic entrepreneur. However, it could cause crowding-out in the market, increased competition for local companies, and over-dependence on foreign enterprises. The evolution of FDI policy in India will be reviewed, empirical evidence analysed in major sectors of the economy, including manufacturing, information technology, retailing, and renewable energy, and the spill-over effects of FDI analysed on domestic investment and entrepreneurship. The results indicate that while FDI has a positive impact on capital formation and entrepreneurship, the effects can be maximised by means of other domestic policies, regulatory systems, and by means aimed at protecting and promoting local enterprises. This paper concludes with a series of policy recommendations aimed at balancing the inflow of foreign investment with the promotion of domestic entrepreneurship, leading to economic growth.

Keywords: Foreign Direct Investment (FDI), Domestic Investment, Entrepreneurship, Economic Growth, India, Multinational Corporations (MNCs).

1. INTRODUCTION

Foreign Direct Investment has taken on a role, as a catalyst for economic expansion especially in fast-growing economies such as India. In terms FDI is when a company or an individual places capital into business activities beyond its borders and it brings not just money but also new technology, seasoned managerial know-how and gateways to international markets. For a nation like India, which launched sweeping liberalisation reforms in 1991¹ FDI serves both as a stream of capital and as a conduit, for weaving the country tightly into the global economy.

India's dance, with foreign direct investment mirrors the swing toward liberalizing capital flows shifting from a tight-fisted stance before 1991 to an open sector-by-sector playbook in the years that followed. Today the subcontinent sits comfortably among the world's FDI hubs pulling in funds for everything from information technology and manufacturing to e-commerce, pharmaceuticals and clean-energy projects. For policy architects foreign capital is more, than a boost; it acts as a catalyst that can ignite spending,

¹ N. Kumar, "Has India's Relative Attractiveness as a Host of FDI Improved?" 33 *Economic & Political Weekly* 1171 (1998).

spark job creation and nurture entrepreneurial energy through the spill-over of knowledge and technology. The relationship, between investment and home-grown investment and entrepreneurship is anything but simple. On the one hand FDI can draw in capital by upgrading infrastructure lifting productivity and opening business avenues. On the hand an overabundance of foreign money risks pushing out firms tightening market concentration and throttling the rise of home-grown entrepreneurship. Getting a handle on this trade-off is key, to shaping policies that capture FDI's upside while curbing its downsides.

The purpose of this paper is to gauge the repercussions of investment, on India's domestic investment and entrepreneurial landscape weaving together theoretical insights and empirical evidence. It delves into the channels through which FDI feeds capital formation sparks innovation and fuels entrepreneurial activity across sectors. Moreover the analysis surveys the evolution of India's FDI policy regime appraising its capacity to drive expansion while bolstering home-grown enterprise development.

This study's reach stretches, across patterns and deep-dive sector-level case analyses aiming to paint a detailed picture of how foreign direct investment, domestic capital and entrepreneurship mesh together. It also points to policy tools that could boost the spill-over effects of FDI while damping any downsides for businesses. By doing it hopes to add a voice to the ongoing conversation, about how India might deliberately leverage foreign investment to fortify its internal economy.

2. Framework of Theories and Concepts

2.1 Definition of FDI

Foreign Direct Investment (FDI) is an investment undertaken by a company or person for shares or business interests, based in another country, where control of the investment and a stake of at least 10% of the equity of the companies concerned is involved.² Direct Investment (as distinct from portfolio investment, which is mainly financial and of a short term nature), involves a continuing interest in and control of the foreign enterprise. FDI may take the form of the establishment of new operations, the acquisition of existing businesses, or the establishment of a joint venture with firms in the host country.³

2.2 Categories of FDI

FDI is usually classified into three main types:

Greenfield Investment: The establishment of new operations or factories in the host country from the outset. This results in the establishment of new employment opportunities and infrastructures, thus contributing in a direct way to economic growth.⁴

Brownfield Investment / Mergers & Acquisitions: An acquired firm or merger with a firm in the host nation. This means quickly activating foreign investment in the country but may be detrimental in that technology is not transferred or local businessmen do not participate.⁵

Joint Ventures / Strategic Alliances: These entail the collaboration of foreign firms and domestic firms for the purposes of sharing resources, technology or management. This type improves the likelihood ideal of spillover effects and entrepreneurial growth.⁶

² U.S. Bureau of Labor Statistics, *FDI Technical Notes* (n.d.), available at: <https://www.bls.gov/fdi/technical-notes/home.htm> (last visited on Nov. 9, 2025).

³ OECD, *Benchmark Definition of Foreign Direct Investment (4th edn., 2008)* (OECD Publishing, Paris)

⁴ Investopedia, *Greenfield Investment Definition* (Investopedia, New York, 2025) (accessed via <https://www.investopedia.com/terms/g/greenfield.asp>) (last visited on Nov. 9, 2025).

⁵ ResearchFDI, "What are Mergers and Acquisitions?-FDI" (ResearchFDI, 2023) (accessed via <https://researchfdi.com/what-are-mergers-and-acquisitions-fdi/>) (last visited on Nov. 9, 2025).

⁶ Fiveable, "Types of Foreign Direct Investment to Know for Multinational ..." (Fiveable, 2023) (accessed via <https://library.fiveable.me/lists/foreign-direct-investment-types>) (last visited on Nov. 9, 2025).

2.3 Theories of FDI

There are several economic theories determining the relationship between Foreign Direct Investment, domestic investment and entrepreneurship:

Dependency Theory: This theory suggests that in general that foreign investment is detrimental in that the country is over reliant on multinationals and may cause domestic firms to be displaced, leading to a parallel situation whereby entrepreneurs become inhibited. The critics of this theory state: while there is something to be said clearly for a degree of growth, seasoning and careful nurturing on behalf of indigenous economic development, there are also strong arguments against dependence on Foreign Direct Investment with its obvious disadvantages in the longer term.⁷

Growth Pole Theory: This theory suggests FDI is a spur to regional and sectoral development. Thus, FDI, through the introduction of capital, technology and management expertise is, in fact, a catalyst for domestic investment and entrepreneurship with all the subsequent positive spillover implications there from for the economy as a whole, both macro and micro.⁸

Endogenous Growth Theory: States that knowledge, innovation and human capital are the prime movers of economic expansion. FDI helps by giving expertise in the form of technology transfer, training and exposure to global best practices, thus furthering entrepreneurship spirit in local firms and innovation.⁹

Theories of Spillovers: The existence of benefits may accrue to domestic firms, arising out of foreign direct investment in the host nation by way of better technology access, better production know-how, better management excellence, to iterate but a few. This means increased productivity, continuity of making fresh ventures, endogenous entrepreneurial growth.¹⁰

3. The FDI Policy Framework in India

3.1 Current FDI Policy

Today India has a relatively liberalized approach to the FDI system and a liberalized approach to policies to attract strategic as well as portfolio investors. The major aspects of the current framework are as follows: **Automatic Route vs Government Route:** FDI in the case of most sectors is permissible under the automatic route without prior clearance. Investments in sensitive or strategic sectors such as defence or telecom require Government clearance.

Sectoral Caps: The system imposes different sectoral caps for foreign equity. For instance, in single-brand retail, up to 100% FDI is allowed but in multi-brand retail the participation is restricted to 51%. Similarly, the defence sector allows for foreign participation of up to 74% under the Government route.

Incentives and Ease of Doing Business: The Indian Government offers tax incentives, infrastructure support, special economic zones (SEZ) to encourage foreign investment. There has also been liberalization of the whole process of regulatory clearance, bureaucratic hurdles are presented in soft form and there is

⁷ Abyssinia Abay, "The Dependency Theory on Foreign Investment" (Abyssinia Law, Aug. 26, 2021).

<https://www.abysiniaweb.com/study-on-line/investment-law/the-dependency-theory-on-foreign-investment> (last visited on Nov. 09, 2025).

⁸ S. Roy, "Empirical Evidence on the Relationship between Foreign Direct Investment and Economic Growth in Selected Asian Economies" 52 *Seoul Journal of Economics* 415 (2012).

⁹ M.A.A. Osuna, "Human Capital Formation and Foreign Direct Investment" 4 *Journal of Economics, Finance and Administrative Science* 72 (2016).

¹⁰ Z. Liu, "Foreign Direct Investment and Technology Spill-overs: Theory and Evidence" 85 *Journal of Development Economics* 176 (2008).

also an improvement in digital platforms available for application for and compliance of these processes.¹¹

3.2 Sectoral Focus

FDI into India has focused on specific sectors in which there is a great promise of growth and technological advancement. The main sectors in which there is ample foreign investment are:

Information Technology and IT enabled services: due to abundance of available talent and global requirement for the same.

Manufacturing: to cater to its various initiatives such as Make in India.

Retail and E commerce: allowing foreign brands to enter Indian marketplace.

Renewable Energy: appearing to be a strong area of commitment from India for sustainable development.

Pharmaceuticals and biotechnology: due to readily available skilled personnel, research, and development.

3.3 Comparative Perspective

With the help of the FDI policy framework in India, in comparison with the policies adopted by other emerging economies, India manages a balance between both the requirements of liberalization as against requirement of domestic protection. While countries such as China adopted a more aggressive approach towards attraction of FDI, starting with special economic zones, from the beginning, India's approach has been cautious and sector focused, and has laid stress on development of indigenous entrepreneurs. This is done so as to obtain maximum benefits of foreign capital while avoiding the adverse impact of foreign industry on local industry.

3.4 Policy Implications

The changing FDI Framework again reflects the intent of the Government to employ Foreign Investment for the purpose of sustainable growth. By giving a balance between liberalization and regulation, it is the intent of the Indian Government to encourage an increase in domestic capital, entrepreneurship, and technology transfer, while at the same time maintaining its priorities for the national economy and preventing excessive foreign influence on domestic industry.

4. Impact of Foreign Direct Investment on Domestic Investment

Foreign Direct Investment (FDI) is significant in determining the patterns of foreign investment in an Indian economy. With help of generation of capital, import of technology and managerial skills, Foreign Direct Investment can generate economic activities and promote the expansion of local unit. This impact is of manifold nature and comprises both advantageous and disadvantageous nature.

4.1 Advantages of Foreign Direct Investment on

4.1.1 Capital Formation

The impact of FDI has proved to be beneficial in several ways and one of them is capital formation. The inflow of foreign capital leads to the additional availability of the capital of the local industrial units which helps them in investing the amount on new set of projects, revision of infrastructure and introduction of modern production techniques etc. For example, FDI in manufacturing sector has led to generation of new units which have increased the overall production and better administration of the production. This capital resulting from FDI may also have multiplier effect by further inviting investments from local companies and financial institutions to members of public.

4.1.2 Transfer of Technology and Skill Development

Foreign Direct Investment brings advanced technology and managerial skills to the country due to which

¹¹ Department for Promotion of Industry and Internal Trade, *Consolidated FDI Policy* (15 Oct. 2020) (Ministry of Commerce & Industry, Government of India).

productive efficiency of local firms can be enhanced. The exposure of local investors to advanced production techniques as well as the latest know-how in terms of the modern managerial world helps local entrepreneurs upgrade their production methods, innovativeness, supply of products and expansion of their production units etc. Sectors like, information technology and drug industry has been instrumental in generation of adequate skilled labour due to the extensive investment and transfer of techniques and knowledge from the foreign companies which provide a better competitive edge to the local investors.

4.1.3 Crowding-in Effect

While the prevalence of foreign investment could lead to fears of foreign investment dominating our markets, FDI can have a “crowding-in” effect, whereby local companies invest alongside foreign investors, taking advantage of the new opportunities afforded to them. Domestic investment often accompanies joint ventures and strategic alliances due in part to better access to foreign markets (including supply chains and networks) and a general development in the overall ecosystem for growth.

4.2 Potential Negative Consequences

4.2.1 Crowding-out of Domestic Companies

While FDI does afford new capital to the market; it can lead to a crowding-out effect particularly in sectors where foreign companies are allowed to take a large role. This crowding-out effect is illustrated in the sectoral growth of domestic companies likely to occur, in some sectors, if an FDI company dominates that market. Thus, it may lead to fewer opportunities for local investors on the part of domestic companies looking to enter or expand in certain sectors, which will lead to a lesser overall national domestic investment habit.

4.2.2 Market Concentration

Where there are high degrees of FDI in certain sectors such as retail, e-commerce and the like, there might be market concentration that will lead to lesser competition and barrier to entry on the part of smaller domestic investors in such sectors. For instance, large foreign companies coming into such sectors may dominate the share of the markets involved, leading domestic companies having a challenge in developing their business.

4.3 Empirical Evidence in India

Since the liberalization of the economic environment in India, the growth in the amount of FDI employed in India has shown high growth from about USD 3.00 million in 1991 to more than USD 80 billion in recent years.¹² Empirical studies have shown that there has been a relatively high increase in the sectors of IT, manufacturing and clean energy (renewable energy) in terms of the increased amounts of domestic investment after large inflows of FDI. For instance, the inflows of FDI into IT sectors have allowed for the locals to expand their software companies, hire a further group of qualified workers and invest in R & D initiatives. In addition to this, we see that the infusion of FDI into the manufacturing sector has also given further impetus for local suppliers to appear in the value chains from those who have entered the sector of manufacturing and substantially increased the domestic amount of investment.

4.4 Sectors under Consideration

Manufacturing: The introduction of greenfield investments has led to increased domestic investments in

¹² India Brand Equity Foundation (IBEF), *India Records Rs. 6,93,864.5 Crore (US\$ 81.04 Billion) FDI Inflow in FY25* (2025), available at: <https://www.ibef.org/news/india-records-rs-6-93-864-5-crore-us-81-04-billion-fdi-inflow-in-fy25> (last visited on Nov. 9, 2025).

the areas of manufacturing facilities, machinery, and logistics.

Information Technology: The technology inflows involved in FDI have allowed for the local startups to also benefit by increased creativity and ultimately look at going abroad.

Renewable Energy: FDI has led to increased domestic investment in areas of solar and wind power plants, with a definite benefit in the growth of the clean energy initiatives presently being instituted in India.

Retail and E-commerce: The inflow of FDI has, no doubt, introduced English practices that have been beneficial and user-friendly. At the same time the governments feel that FDI has led to problems with the smaller SMA companies who have earlier expressed concerns over the prevailing conditions.

5. Influence of FDI on Entrepreneurship

Foreign Direct Investment (FDI) provides not only funds to the host economy but also affects the entrepreneurial scenario by creating new opportunities, new skill sets and new combinations in its market. In India, FDI has had a positive impact as well as a negative influence on the domestic entrepreneurship which encompasses start-ups, small and medium enterprises (SMEs) and new innovations in various sectors.

5.1 Positive Influence on Entrepreneurship

5.1.1 Knowledge and Technology Spill-overs

One of the most vibrant areas of entrepreneurship, to which FDI has contributed significantly, is the transfer of knowledge, technology and managerial practices from multinational corporations (MNCs) to domestic enterprises. The local entrepreneurs have the exposure to global standards, efficient production techniques and innovative business models, which are stimulus for new ventures and enhanced competitiveness. For instance, the FDI in IT and pharma sectors has endowed the local start-ups with advance technological support for the production of products and services of international quality.

5.1.2 Market Access and Networking Opportunities

FDI introduces the local entrepreneurs to global supply chains, global markets and business networks. The local start-ups have an opportunity to expand their market beyond the borders of the country, which offers abundant opportunities for them to cater to foreign clientele, by developing Joint ventures or partnerships with foreign enterprises which promote the marketing of global techniques to the domestic producers. These factors increase the opportunities of expansion to local enterprises and give birth to new inventive ventures oriented towards international requirements.

5.1.3 Availability of Capital

FDI can indirectly create atmosphere conducive to entrepreneurship. The increase of the flow of funds from foreign sources, increase in liquidity and opportunities of attracting more venture capital and private equity funding. Domestic entrepreneurs receive easier access to finance which enables them to set up businesses or improve existing businesses, to invest in innovation and to expand capacity.

5.1.4 Fostering Start Ups and SMEs

FDI has stimulated development of startup eco-system in India which is emerging particularly in technology driven sectors. The e-commerce and fintech industries have received foreign investments which have encouraged the domestic startup industry due to mentoring, collaboration and exposure to international best practices. Investments in start-up companies can create a domino effect which will encourage entrepreneurial talent, which can be encouraged in an eco-system in which smaller businesses flourish alongside established foreign competition.

5.2 Challenges to Domestic Entrepreneurs

5.2.1 Increased Competition

Foreign companies will have their benefits but they will also increase competition in the domestic market. This has varying consequences. Domestic entrepreneurs and smaller companies are greatly affected by increasing competition in their sectors by established, well funded multinational companies with their advantages through economy of scale, perhaps a more developed technology and their global brand names. Increased competition can restrict the growth of smaller companies and also curtail entrepreneurial projects from prospective entrepreneurs.

5.2.2 Dependence on Foreign Firms

Too great a dependence on foreign technology and foreign partners can lead to a situation of dependence for domestic entrepreneurial talent. Startups and SMCs are more likely to develop their area of interest along the lines of dependence and interest with possible foreign financial partners rather than fostering their innate projects of self-sufficient indigenous growth ideas which could inadvertently lead to entrepreneurship models which do not encourage indigenous concepts.

5.3 Sectoral Examples in India

Information Technology: FDI investment has been directed towards IT enabled services. The end result is the development of numerous domestic software service start-ups and resultant increased software exports and global competitiveness.

E-Commerce and Retail: The influx of foreign investment and in the infrastructure and logistics development has seen the establishment of highly competitive retail operations with established foreign competition against the local entrepreneurs.

Renewable Energy: Energy projects particularly solar and wind developments have encouraged entrepreneurial projects in India, due to the entry of foreign funds in these technologically oriented sectors, including the pursuit of technology and ultimately the escalating importance of government policy inputs.

Pharmaceuticals and Biotechnology: In these two sectors, foreign investment in projects in collaboration with Indian entrepreneurs has led to an acceleration of research and development and the emergence of a biotechnology start up culture.

5.4 Empirical Evidence

Research indicates that FDI flows often bear a positive relation to entrepreneurial activity and growth in sectors of industry where a high role is played by technology transfer and managerial experience.¹³ The information technology, renewable energy and pharmaceutical sectors have seen high degrees of foreign FDI interest which has resulted in increased startup companies, enhanced degrees of new ideas being tested and pursued, in marketing and improved business techniques. In the retail and large scale manufacture sectors however, results are mixed. The regulatory climate is a hugely important factor in the support of domestic entrepreneurship.

6. Implications, for Policy

The way foreign direct investment (FDI) weaves into India's investment and entrepreneurial fabric is

¹³ S. Choudhury, S. R. Kumar and Brajesh Singha, "Foreign Direct Investments and Its Impact on Entrepreneurship in India" 26 *International Journal of Entrepreneurship* (2022), available at: <https://www.abacademies.org/articles/foreign-direct-investments-and-its-impact-on-entrepreneurship-in-india-15030.html> (last visited on Nov. 9, 2025).

anything but simple. On the one side FDI pours in capital ushers in cutting-edge technology sharpens workforce skills and stretches market reach. On the side it can tighten market concentration, sideline home-grown firms. Ratchet up competitive pressure, for local entrepreneurs. Getting a sense of these intertwined forces is vital, for shaping policies that capture FDI's upside while tempering its drawbacks.

6.1 Bringing the Key Findings Together

Foreign direct investment tends to lift investment through pathways. It channels capital into priority industries nudges upgrades of infrastructure and drives productivity gains. In the IT manufacturing and renewable-energy arenas domestic firms typically react to FDI by stepping up their spending and embracing cutting-edge technologies, a pattern economists label the "crowding-in" effect.. The story flips in sectors where foreign companies hold sway, like multi-brand retail, where heightened competitive pressure can dampen firms' appetite, for fresh investment.

In the arena foreign direct investment acts as a source of knowledge spillovers, seasoned managerial know-how and a gateway, to international markets.¹⁴(Behera et al., 2012) Start-ups and SMEs operating in IT, e-commerce, pharmaceuticals or renewable energy reap the benefits of partnerships, joint ventures and exposure to practices. Still the upside comes with strings attached: an over-reliance on partners the market-dominance of multinationals and a limited capacity among entrepreneurs to absorb new ideas all underscore the need, for carefully targeted policy measures.

6.2 What This Means, for Policy

To squeeze the most out of investment, for bolstering domestic capital flows and nurturing entrepreneurship policymakers should hone in on the following strategies:

Sector-Specific FDI Policies: capital, toward industries that dovetail with national strengths—renewable energy, information technology and pharmaceuticals—while imposing prudent controls on segments where domestic firms could be sidelined.

Support, for firms: unleash a blend of tax breaks grant programs and credit access tailored for SMEs and nascent startups so they can square off with competitors on a level playing field.

Technology and Knowledge Transfer: Make it mandatory, for sectors that draw direct investment to launch collaborative knowledge-sharing initiatives thereby harvesting spill-over effects and fueling home-grown innovation.

Entrepreneurial Ecosystem Development: Seed the ecosystem with incubation hubs nurture emerging founders through mentorship initiatives and shape a policy landscape that welcomes startups thereby converting the benefits of FDI into growth.

Monitoring and Regulation: Sustain a mix that thwarts monopoly tendencies while preserving an equitable arena, for both foreign and home-grown enterprises.

6.3 Implications, on a scale

The way foreign direct investment, domestic investment and entrepreneurial activity intertwine holds sway, over Indias growth blueprint. By courting FDI and aligning it with home-grown policies India can speed up industrial expansion raise productivity and nurture sustainable entrepreneurship. This combination not bolsters the economy but also casts India as a more competitive contender, on the world stage.

All told foreign direct investment can serve as an engine, for progress yet its upside hinges on well-crafted

¹⁴ S. Ranjan Behera, Pami Dua and Bishwanath Goldar, *Technology Spillover of Foreign Direct Investment: An Analysis of Different Clusters in India* (2012), available at: <https://mpr.ub.uni-muenchen.de/43840/> (last visited on Nov. 9, 2025).

policies a strategic focus on the right sectors and vigorous support, for domestic investment and entrepreneurship.

7. Conclusion

Foreign Direct Investment (FDI), is now an important aspect of India's Economic Development Strategy and has been shown to drive economic growth, improve productivity and promote India's integration into the global economy. This paper presents the various implications of FDI on Domestic Investment and Entrepreneurship and highlights how FDI can be seen as a driver for domestic investment and also how FDI can hinder local entrepreneurs.

As stated earlier, this paper found that FDI provides significant contributions to Capital Formation, Technology Transfer and Skill Development and creates a "Crowding In" effect which promotes Domestic Investment. The paper also states that FDI has promoted entrepreneurship through providing greater market opportunity, improving access to financing and promoting innovation through Knowledge Spillovers. However, the benefit from FDI is not equally distributed across all sectors and excessive foreign control can place a high degree of competitive pressure on small local firms reducing their ability to grow as Indigenous Entrepreneurs.

To allow India to achieve the full potential of FDI, Policy Makers must provide a balanced approach to FDI by being open to Foreign Investment while protecting and promoting Local Enterprises. To achieve these objectives, Policy Makers must strengthen Regulatory Frameworks to support Small to Medium Sized Enterprises, ensure Technology Transfer occurs effectively and ultimately create an environment where FDI will contribute to Sustainable Growth and Innovation in Entrepreneurship in the long-term future.

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