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Review Paper

A Study of Indian Multinationals and Public Enterprises in Abroad: A Preliminary Review

Md Suhail Ahmad[1] and Manoj Kumar Mishra[2*]
[1]-Research Scholar in Management, Magadh University Bodhgaya, India.
[2]-Associate Professor, CFMD, Ethiopian Civil Service University, Addis Ababa, Ethiopia.

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Corresponding Author:
Manoj Kumar Mishra
Associate Professor, CFMD, Ethiopian Civil Service University, Addis Ababa, Ethiopia.

Abstract
Globalization of firms from emerging markets by means of foreign direct investment (FDI) has undergone a rapid transformation in recent years. The phenomenon of outward Foreign Direct Investment (FDI) from developing countries, especially China and India, has attracted global attention in press, academia and policy circles. The purpose of this paper is to examine the motivations behind Indian firms' outward investment, i.e. whether these firms are investing abroad in search of market, resource, technology, strategic-assets, efficiency, etc. Outward FDI by Indian firms has increased considerably in recent years. Such investments have gone to more than hundred host countries and into various sectors. The higher volume of outward FDI following policy reforms requires examination of factors that have motivated Indian firms to invest in different host countries. The study is based on exploratory research design using the secondary data. The facts and statements have been analyzed in logical ways. . This study finds that capital outflow is increasing and its direction is shifting from developing to developed nations; from manufacturing to knowledge based sector and ultimately Indian multinationals will sustain in the global market.

Keywords: *Outward FDI, Capital Flow, Economic reform, Globalization, Indian multinationals.*

Introduction

Globalization of firms from emerging markets by means of foreign direct investment (FDI) has undergone a rapid transformation in recent years. Starting from humble beginnings around the 1960s, a number of emerging markets have become leading outward investors during the first decade of the twenty-first century. Average outward FDI (OFDI) flows from these new sources of direct investment have grown from just US$348 million in the 1970s to over US$170 billion in the first decade of the twenty first century; in 2008, OFDI flows from emerging markets reached US$350 billion. Emerging markets recorded a 57% growth rate of OFDI flows in the period 2000–2008, which is about double the OFDI growth rate of developed countries. This constitutes a sharp increase in the growth gap of OFDI between emerging markets and developed countries beginning in the 1990s, when the growth rate of emerging markets was merely 1.2 times the growth rate of developed countries, compared to two times the growth rate during the 2000s.

The phenomenon of outward Foreign Direct Investment (FDI) from developing countries, especially China and India, has attracted global attention in press, academia and policy circles. This is due to China being the largest outward investor amongst the developing countries in recent times, whereas India, although behind Russia and Korea, has got the attention of global economic community as a result of significant growth in the volume of outward FDI since the gradual liberalization of capital account restrictions starting form the introduction of Foreign Exchange Management Act in the year 2000. The growing economic significance and changes in the trajectory of economic growth of the country have also *"attracted attention of international community"*. These countries being latecomer, in terms of investing abroad, continues to impress the world community with multi-billion-dollar investments, either Greenfield or merger and acquisition. The outward FDI of Indian firms are increasing in abroad and these firms are being competitive in foreign. The trend of investment is also changing from manufacturing to knowledge based industries. Now Indian firms are capable to compete in developed countries but in global competitive environment, the study of trend is very important for sustaining the Indian multinationals. Therefore, it is required to study the performance of Indian multinationals in abroad. The objective of this paper is to find out the trend of outward foreign Direct Investment of India in recent years. It also finds out the direction of investment, performance, capital outflow, and future of Indian outward FDI.

Review of Literature

The emergence of Indian firms investing abroad can be traced back to the early 1960s. The setting up of a textile factory by the Birla Group in Addis Ababa, Ethiopia, in 1960, as well as a wholly owned trading subsidiary by the Tata Group in Zug, Switzerland, in

1961, marked the beginning of OFDI from India. Other industrial houses like Thapar, JK Singhania, Maftlala, and Godrej joined in later. Indian firms were pioneers among developing countries in undertaking OFDI, with essentially a small group of family-owned business groups engaging in modest investments in selected developing countries from the 1960s to the 1980s. Public-sector companies largely remained outside the process of OFDI in this period, except in a small number of cases. Host developing countries—led by Southeast Asia, East Africa, the Commonwealth of Independent States (CIS), and West Africa—accounted for about 82% of cumulative Indian OFDI flows during the period 1960– 1989. The number of outward-investing Indian firms rose from 11 in the 1960s to 146 in the 1980s. During this phase, public policy, development levels, geopolitical alliances, and evolving corporate strategies shaped and determined the nature of Indian OFDI (Pradhan 2008, United Nations Conference on Trade and Development 2007). State regulation of the growth of large industrial houses motivated, for the most part, the OFDI decisions of Indian firms. These business groups had enjoyed rapid expansion at home. The scope for further growth was limited due to the slow expansion of the domestic market and the existence of restrictive regulatory measures like the Monopolies and Restrictive Trade Practices Act, 1969 (MRTPA), the Foreign Exchange Regulation Act, 1973 (FERA), and industrial licensing. Indian policy makers, acknowledging the potential of OFDI for promoting national exports and for strengthening development cooperation with other developing countries, selectively allowed overseas operations of Indian firms. Inadequate foreign exchange reserves, together with the weak expertise and knowledge of Indian firms, led to an OFDI policy regime that permitted overseas investments only through exports of Indian-made machinery, and through know-how against cash transfers (and in the shape of ownership control through joint ventures [JVs]). Developing regions that had cultural, geographical, and ethnic proximity to India became the primary destinations for outward investment for Indian firms that intended to capitalize their limited knowledge and simple ownership advantages, as shown indiagram. The manufacturing sector, mostly confined to a few select industries like chemicals, paper, and textiles, dominated the sectoral distribution of Indian OFDI during 1961–1989.

Outbound investments from India have undergone a considerable change not only in terms of magnitude but also in terms of geographical spread and sectorial composition. Analysis of the trends in direct investments over the last decade reveals that while investment flows, both inward and outward, were rather muted during the early part of the decade, they gained momentum during the latter half. There has been a perceptible shift in Overseas Investment Destination (OID) in last decade or so. While in the first half, overseas investments were directed to resource rich countries such as Australia, UAE, and Sudan, in the latter half, OID was channelled into countries providing higher tax benefits such as Mauritius, Singapore, British Virgin Islands, and the Netherlands.
Indian firms invest in foreign shores primarily through Mergers and Acquisition (M&A) transactions. With rising M&A activity, companies will get direct access to newer and more extensive markets, and better technologies, which would enable them to increase their customer base and achieve a global reach.

As the developing countries are becoming increasingly active in terms of cross border investments, the locational determinants of their outward FDI warrant considerable attention. In the light of the eclectic paradigm a number of host country factors can be identified that might explain developing country firms' outward FDI in different host countries. These factors include (but not limited to) natural resources, low labour and input costs, large markets, intangible assets such as endowment of technology and strategic-assets, legal and commercial environment. Each of these locational factors can be linked to a particular motive of outward investment by the firm. The locational advantages could differ significantly in different host countries. In addition, firms could have single or multiple motives for investing in different host countries, i.e. firms may integrate different possible motives while deciding to invest in different host countries. For analytical convenience, it is possible to classify the locational factors under different headings, based on taxonomy developed by UNCTAD (1998, p. 91), Dunning (2006, p. 206). Accordingly, a few important motives have been classified as under.

Firms tend to invest in countries that have larger market size due to higher expected demand for its products. The market-seeking FDI can also materialize when the firms try to increase their global footprint by entering new market, to explore business opportunities abroad, to expand brand in the global market and to diversifying across different overseas markets. Market-seeking FDI, which is horizontal in nature, will grow in importance in the context of higher growth potentials for the firm in the foreign market vis-à-vis in the domestic market. Several studies have found evidence of market-seeking FDI (Chakrabarti, 2001 for cross-section of countries; Cheung and Qian, 2009 for China; Mottaleb and Kalirajan, 2010 in developing countries; Goh and Wong, 2011 for Malaysia; Kolstad and Wiig, 2012 for China; Ramasamy et al., 2012 for Chinese private firms; Nunnenkamp et al., 2012 for India). There are also several recent examples of market-seeking outward FDI by emerging multinationals from India. Bharti Airtel Ltd. acquired Zain Africa BV in 2010 to enter into the African market, i.e. through the acquisition route. Similar recent instances of market-seeking outward FDI by Indian firms include the following investments by (in joint venture/wholly owned subsidiary) Wipro Ltd. (EN Think Inc, USA; Wipro Chengdu Ltd., China), Infosys BPO Ltd. (Mccmish Systems LLC, USA), HCL Technologies Ltd. (HCL Technologies (Shanghai) Ltd.), Mahindra & Mahindra Financial Services Ltd. (Mahindra Finance USA LLC), Kerala Ayurveda Ltd. (Ayurvedic Academy Inc., USA), Gitanjali Gems Ltd. (Gitanjali USA Inc.) etc.

This expansion of OFDI from emerging markets is driven by the rise of firms from Asian developing economies. During the 1970s, when FDI outflows from emerging markets were modest, Latin American and African firms were ahead of their Asian counterparts in terms of average OFDI values and their percentage share of total outflows from emerging markets their share in emerging market OFDI flows jumped above 70% during the 1980s and 1990s, and then leveled out at 62% in the 2000–2008 period. Conversely, Africa's share in OFDI flows from emerging markets declined from 37% to 3% between 1970 and 2008, and the share of Latin

America dropped from 61% to 18% during the same period. Clearly, the geographic concentration of OFDI flows from emerging markets has raised, with developing Asia emerging as, by far, the dominant home region for OFDI by emerging market multinational enterprises (MNEs). Among the emerging Asian economies, the overseas expansion of Indian firms has been quite noticeable. Although firms from China, Hong Kong (Special Administrative Region of China), the Republic of Korea, Malaysia, the Philippines, Singapore, and Taiwan, Province of China, continue to lead in terms of OFDI flows from emerging Asia, the growth of OFDI from India has been the third highest after the United Arab Emirates and Egypt during 2000–2008.

Discussion

Indian OFDI flows have grown dramatically since the 1990s. The volume of OFDI flows increased from just US$152 million in the period 1980–1989 to US$3.4 billion in the period 1990–1999, and further to US$37 billion between 2000 and 2007. The corporate picture of Indian OFDI became more complex, with the number of outward-investing Indian MNEs jumping from 146 in the period 1980–1989 to 1,257 in 190-99 and 2,104 in 2000-2007. The rapid growth of Indian OFDI flows during the 1990s and the first decade of the twenty-first century has been associated with a broadening of the industry and the geographical profile of investments. Current OFDI flows from India reflect a broad industry composition, including the rise of new players from industries as diverse as gas and petroleum, software, and pharmaceuticals. The surge in Indian OFDI since the 1990s, and its various new features, appears to be a result of the interactions among changes in national policy, corporate behavior, and international developments in trade and investment. The removal of the restrictive measures on the growth of firms (like FERA), the removal of the licensing regime, the dismantling of product reservation systems for public-owned and small- and medium-sized enterprises, facilitative measures for foreign firms, and a massive reduction in import duties all led to intense competition in Indian markets. Most of the large Indian firms were seriously affected by growing competition, and were restructured to emphasize product specialization, increase productivity, and improve product quality.

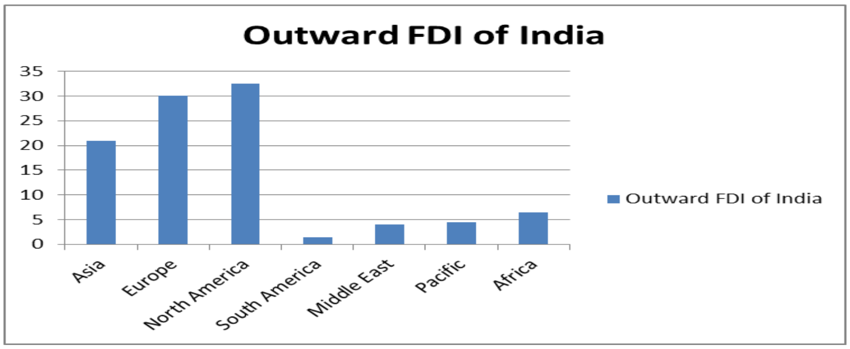

Fig. 1 Outward FDI of India. *Source: Calculated from RBI data*

These domestic firms had inherited reasonable but inefficient industrial expertise, skills, and traditions from an inward-looking policy regime that encouraged localization of production and import substitution. By implementing new corporate measures—to beat the competition in the 1990s—Indian firms appear to have improved their competitive strength, leading to improved bottom lines and higher levels of liquidity. In anticipation of the introduction of stricter protection of intellectual property, many Indian firms gravitated toward higher in-house research and development (R&D) activities in the late 1990s, and toward external acquisitions of technologies in the first decade of the twenty-first century. The reason is that regions with higher stages of development play host to firms that are based on powerful and broad-based monopolistic advantages originating from Schumpeterian frontier innovation, sophisticated product differentiation, and specialized management and managerial skills. There appears to be a sectoral dimension to this geographic specialization. As Indian MNEs' entry into developed regions is spearheaded by the services sector, while their entry into developing regions is led by the manufacturing sector, the probability of an Indian firm being a developed region-specific Indian MNE is higher if it is from the services sector. In the case of the software and information technology (IT) industry, Indian MNEs are overwhelmingly developed-region specific, because developed countries are the primary source of demand for these services. This issue could also gain from a rigorous empirical analysis that the existing literature on Indian MNEs is still lacking.

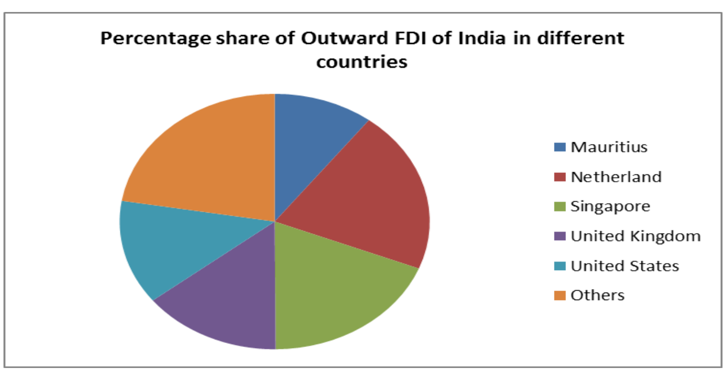

Fig. 2. Share of FDI. *Souce: Calculated from RBI Data*

Over the years, Indian OFDI has become diversified over different industries, and is increasingly being led by knowledge-based industries in the manufacturing and service sectors. For a developing country with a labor surplus, to have a greater share of its OFDI in technology- and skill-intensive industries is a truly interesting phenomenon that deserves to be further investigated: is this recent surge in knowledge-intensive OFDI reflective of some competitive advantage of India in the industries concerned? India has been successful in promoting an indigenous capability through strategic, industrial, and technology policies in industries such as pharmaceuticals, the automotive industry, and IT. There exists ample documentation to show how the Indian government has used an active industrial policy and a liberal patent system to encourage domestic investments in pharmaceuticals and in the automotive. The objective of this paper is to find out the trend of outward foreign Direct Investment of India in recent years. It also finds out the direction of investment, performance, capital outflow, and future of Indian outward FDI. The growth of the Indian IT industry has been explained by the creation of the required domestic skills, initial demand from the public sector, and a liberal policy regime for inward foreign investment (Pradhan 2010). The depth and competitiveness of Indian firms in these industries increased substantially, with India moving away from a protected regime to economic openness in the 1990s. This improved competitiveness may be partly responsible for facilitating the knowledge-based OFDI of the last decade.

Conclusion

The growth of Indian OFDI from knowledge-based industries ultimately reflects the rapidly improving competitive capabilities of firms in these industries. Indian firms in the automotive and pharmaceutical industries have, in the past, leveraged linkages with foreign firms as a means of gaining technology. Given the current liberal environment, Indian companies are turning to acquisitions to upgrade on the path of technological advancement. However, among emerging Indian MNEs, there exists inter-industry differences in the nature of their firm-specific characteristics. The need to access overseas natural resources has also been one prominent driver of India's OFDI path in recent years. These reflections on the important question of how Indian FDI is faring and how it is affecting host countries deliver new insights that are worthy of further analysis. Indian investment in both the United States and Germany shows a growing bias toward knowledge-intensive industries like software, pharmaceuticals, and the automotive industry.

This paper examined the motivations behind Indian firms' outward investment, i.e. whether these firms are investing abroad in search of market, resource, technology, strategic-assets, efficiency, etc. Outward FDI by Indian firms has increased considerably in recent years. Such investments have gone to more than hundred host countries and into various sectors. The higher volume of outward FDI following policy reforms requires examination of factors that have motivated Indian firms to invest in different host countries.

These are the industries in which India has succeeded in building unique capabilities, sometimes pursuing a strategy of low-cost innovation. Indian OFDI could potentially lead to a more competitive market structure, and to inflows of additional innovative assets. Indian MNEs are increasingly contributing to local R&D (e.g., in the case of Germany), supported by developed countries' strong innovatory infrastructure and skills. Overall, Indian MNEs are net positive contributors to employment and to development in India as well as world in general. This study finds that capital outflow is increasing and its direction is shifting from developing to developed nations; from manufacturing to knowledge based sector and ultimately Indian multinationals will sustain in the global market.

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