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Outward expansion by Indian firms: the European route

Christian MILELLI



UMR 7166 CNRS

Université Paris X-Nanterre
Maison Max Weber (bâtiments K et G)
200, Avenue de la République
92001 NANTERRE CEDEX

Tél et Fax : 33.(0)1.40.97.59.07
Email : secretariat-economix@u-paris10.fr



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C. Milelli

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Abstract

This contribution attempts to shed light on the surge of direct investment flows from India because of the limited understanding of this huge country in the context of liberalization of inward and outward foreign direct investment. As far as the latter is concerned, India cannot be described as an underdeveloped country since it can mobilize substantial native capital and it hosts flourishing multinational companies. The liberalization of the national economy in the early 1990s and the resulting arrival of large foreign multinationals have prompted domestic companies to engage in a restructuring path along with to seek new business opportunities overseas in order to expand market share. If the bulk of Indian outward direct investment is still directed toward developing countries, mature economies are emerging as a growing host place.

The paper focuses on Europe and draws on a wide range of data from various sources, and tackles the question empirically in order to provide a more comprehensive understanding on entry modes and strategies followed by Indian investors.

JEL Classification Numbers: F14, F23

Keywords: foreign direct investment, multinational firm, India, European economies

This contribution attempts to shed light on the surge of direct investment flows from 'third-world' to 'first-world' countries and explain why third world companies are currently investing in advanced economies. This emerging phenomenon has several implications for the host economies and global competition.

To analyze this new trend, we chose to focus on India because of the limited understanding of this huge country in the context of liberalization of outward and inward foreign direct investment (FDI). As far as FDI is concerned, India cannot be described as an underdeveloped country since it can mobilize substantial native capital and it hosts flourishing multinational companies. The liberalization of the national economy and the resulting arrival of large foreign multinationals have prompted domestic companies to engage in a restructuring path along to seek new business opportunities overseas in order to expand market share. But due to an international stage — much more globalised with transnational networks within large multinational in command than previously in the 1980s with the Japanese FDI surge or in the 1990s with the Korean one — Indian companies have to be choosier in terms of strategy. If the bulk of Indian outward FDI is still directed toward developing countries, mature economies are emerging as a new target.

The paper focuses on Europe and draws on investment data and cases from various sources, and tackles the question empirically. It is structured as follows:

First, a statistical analysis of investment data is carried out in order to give an overview of the magnitude of the phenomenon, along with the spatial and sectional distribution of India's direct investment in developed countries;

Second, to take account of the strategies followed by Indian companies on the eve of entering European markets we have collected and construed individual data on those companies. As a result, we draw insights about Indian corporate presence in Europe;

Third and last, we discuss some conjectures which have been put forward about the economic impacts of these investments on European countries.

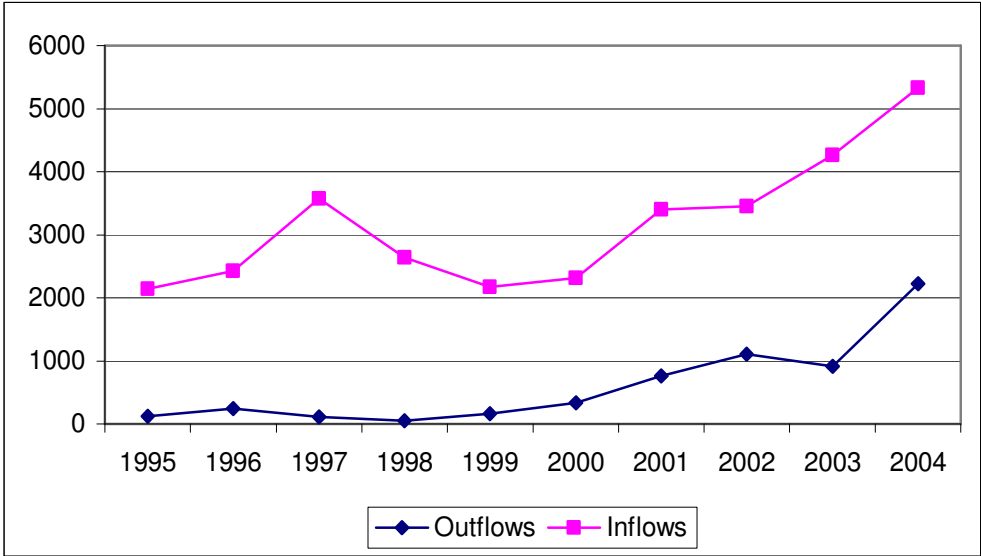
1. Indian direct investment in a worldwide perspective: Basic trends for developed countries — Europe *versus* North America

Even before the independence India was home of vibrant national entrepreneurs and large companies. For example, the well-known Birla group which started cotton trading in the 1850s, or the Tata group which emerged in the 1870s through a textile mill, had sizeable market shares during the 1940s.

Therefore, Indian companies have been investing abroad for many years, but it is only recently, say since 2000, that Indian outward direct investment flows have taken off to reach substantial amounts on an annual basis. The first signs of Indian investments overseas date back to the beginning of the 20th century with cotton-spinning started in Uganda by an Indian investor in 1920 (Jaffrelot 2005), and thereafter in the 1950s with further investments in Africa by the Birla group. The whole picture changed in the 1990s. The underlying factors were the deregulation and liberalization of the Indian economy after a foreign exchange payment crisis which culminated in the early 1990s: previous import licences were given up, tariff trade barriers lessened and impediments to foreign direct investment and portfolio investments were relaxed. However, India's economic policies altered only incrementally. Regarding India's economic growth in 1994, it must be noted that the

Indian government chose not to accept further 'structural adjustment type' IMF loans as had been the case in 1990 (Kohli 2006). This policy orientation explains why FDI outflows stayed almost flat during the second part of the 1990s¹, and it is only in 2002 that the symbolical one billion dollar mark was reached. Accordingly, **Figure 1** exhibits a more synchronous trend between inflows and outflows since 2001 because of a more balanced relaxation of regulations along with growing opportunities for foreign companies to invest in India on the one side, and for Indian companies to start and expand operations overseas on the other.

Figure 1: Indian FDI inflows and outflows, 1995-2004 (in million US dollars)

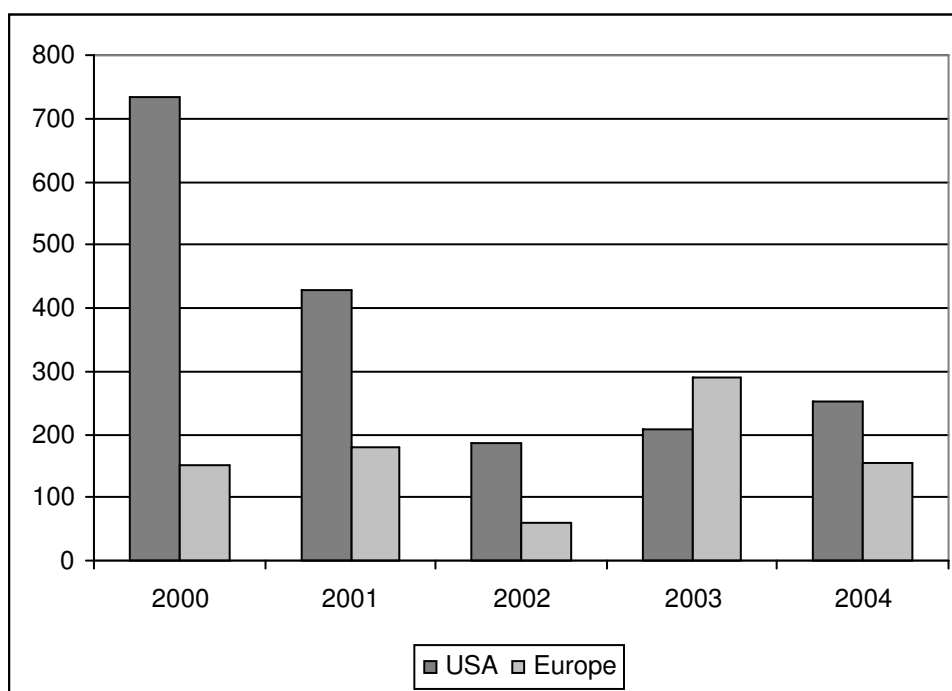


Source: UNCTAD, World Investment Reports/WIR

According to UNCTAD (WIR 2005), the share of Indian FDI to GDP is still modest: it was only 1 percent in 2004 (2.4 percent for mainland China). But Indian data are underestimated as is usually the case with investments coming from developing countries even if India adopted FDI international computing standards in 2001. Developing countries are still getting the lion's share of Indian FDI whereas developed countries received less than 30 percent of the total cumulative outflows for fiscal years 1995-2005 (RBI 2006): the United States accounted for 16.3 percent and Europe for 11.3 percent. However, **Figure 2** is based on notifications and shows Europe catching-up with the United States in the last period.

¹ The following was also part of the explanation: the ending of the domestic market protection policy caused Indian firms to spend large amounts of capital and was followed by a period of consolidation and rationalisation.

Figure 2: Approved Indian outward FDI flows to the United States and Europe, fiscal years 2000-2004 (in million US dollars)



Source: Reserve Bank of India

The percentage of manufacturing activities in Indian FDI flows to developed countries is comparatively smaller than in the total stock of Indian outward FDI, while the percentage of non-financial services and, to a lesser extent, financial services is much higher. This result is consistent with the expansion of services in developed economies, particularly in the United States.

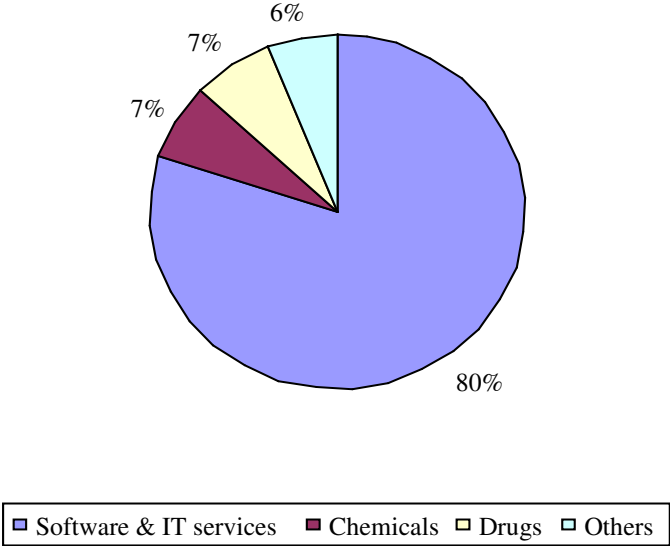
If cross-border mergers and acquisitions (M&As) are currently the usual route for direct investment between developed countries, and represent the bulk of these operations on a worldwide basis, companies from developing countries are also getting on the bandwagon. Furthermore, M&As by Indian firms across Europe and the United States are fully part of these companies' international strategies. It is worth considering this aspect in more detail. To this effect, we used the SDC Platinum database from Thomson financial which tracks these operations worldwide. For the 1999/2005 period we found two interesting results:

First, contrary to the dominant point of view arguing that it is easier for a company that wishes to be quickly operational to enter Europe's markets through M&As while the United States offers a more relaxed environment for setting up new activities, the fact is that Europe and the United States are on an equal footing for the number of M&A deals (Europe: 106, USA: 108).

Second, there is a striking difference between both areas for industry distribution. **Figure 3a** shows a very concentrated distribution in the United States for packaged software and IT services with drugs and chemicals taking the remaining part. Such concentration is due to the mainly services-oriented nature of the U.S. economy, and

the important place taken by outsourcing and off-shoring for the application, development and maintenance of software. Note that, in 2004, more than two thirds of India's software services were exported to the United States.

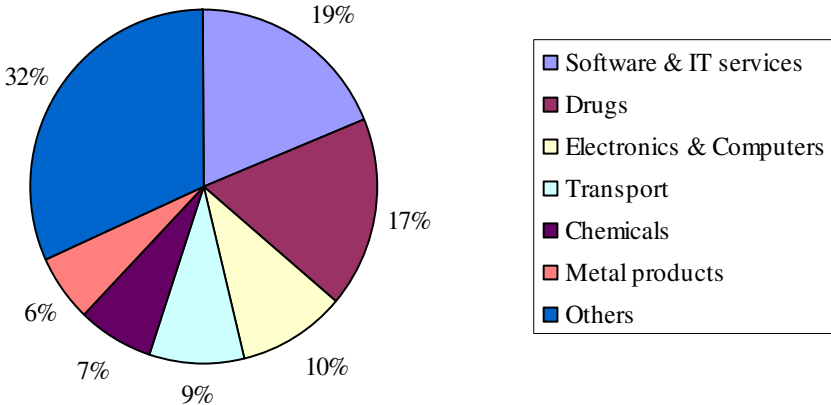
Figure 3a: Industry distribution of M&As by Indian firms in the US, 1999-2005



Source: SDC Platinum database

Conversely, **Figure 3b** displays a larger array of domains for M&A deals by Indian companies across Europe. Software and IT services were in the forefront but at a relatively lower level than in the United States — European companies are still reluctant to outsource activities on the same level as U.S. companies. The importance of drugs can be attributed to the competitive advantage of Indian companies in generics drugs. Moreover, in the European context of national deregulation these companies are willing to capture market share, and the M&A route is obviously the best strategy to advance rapidly inasmuch as large European drugs companies or U.S. multinational affiliates are currently divesting such activities due to low margins. Overall, the larger spectrum can be explained by more fragmented and diversified economies on the one part, and Indian companies' desire on the other to use their competitive advantage to secure fast market share growth in these different sectors, such as electronics and computers, transport, chemicals or metal products.

Figure 3b: Industry distribution of M&As by Indian firms in Europe, 1999-2005



Source: SDC Platinum database

2. The decisive influence of India’s development path

Obviously, the national factors are still interplaying with the globalization on a large extent.

As the common determinant of companies’ decisions to invest overseas — *i.e.* to avoid trade barriers — has lost importance, motivations are now largely based on the assertion of competitive advantage by firms. However, in the case of developing countries like India such advantage hinges upon the path followed by the national economy and its embedded environment.

It is worth recalling that after independence, India focused on self sufficiency to avoid dependence on imports and excessive external influence on its domestic affairs. This view was understandable for a country which had only recently emerged from colonialism. Furthermore, India considered itself an exemplar for other developing countries. Therefore, early emphasis was put on import substitution with stringent trade restrictions. However, contrary to other developing countries, independent India always allowed the development of private sector activity even though tight regulations kept it under strict government control — investment licensing, import licensing, controls on the use of foreign exchange, etc. — as part of the planning framework.

Another Indian characteristic was to give higher education priority over primary education. This remains true today: India spent 86 percent of per capita GDP on each student in tertiary education in 2000 yet only 14 percent in primary education (Kochhar 2006). As a result, the availability of qualified manpower along with selective industrial policies has resulted in a national manufacturing base quite different from that of other developing countries. The Indian situation is indeed characterized by more capital-intensive activities and higher productivity.

The economic reform era which began with small deregulation steps in the mid-1980s and gathered speed in the 1990s had, of course, an effect on the behaviour of Indian firms at both national and international levels. Due to path-dependency inertia however, previous industry specialization is still alive. Deregulation and liberalization simply enlarged the strategic scope: it stimulated the organic growth of national companies in their traditional domains, it encouraged the entry into new sectors through diversification strategies and refocused strategies and specialization. In addition, the repeal of the 1970 Foreign Exchange Regulation Act — which aimed to control capital outflows — has reduced the number of obstacles Indian companies have to override when they wish to invest overseas.

To sum it up, the distributional importance of software and IT services, and drugs in India's FDI flows to developed economies is for a large part due to India's past and present economic environment. Let's now take a closer look at these two sectors.

2.1. Indian software and IT services industry

As a matter of fact, until the mid-1960s, there was virtually no software development in India. The industry actually got its start in 1968 with the establishment of Tata Consultancy Services (TCS), a wholly-owned subsidiary of Tata Group. Yet, TCS only really took off after IBM withdrew from India in 1978.

If the development of the Indian software and IT services industry has been market-driven with minimal government regulation, its growth however was propelled by direct and indirect public incentives. First, it is well-known that in the late 1950s and 1960s the Indian government invested in elite technical institutions, such as the Indian Institutes of Technology and Indian Institutes of Management, as well as a large number of other engineering colleges. These institutions produced abundant talent, a critical input for the software services industry. Second, the government took the initiative by setting up technological parks with fiscal exemption and providing Indian software companies with direct telecommunication access to customers in the United States and Europe. In so doing, the government circumvented the public monopoly of the Indian telecommunication operator.

Also of great importance was increasing international demand for such competitive and skilled manpower — more particularly from U.S. companies. A study observed that Indian software firms now possess strong capabilities in process maturity and management skills, which positively impacts on their international competitiveness (Tschang 2003). Thus, Indian software companies are attempting to move up the value-chain and establish presence in key countries around the world.

Lastly, the outward-looking nature of the industry was influenced from the outset by the unattractiveness of the domestic market. The following reasons can be advanced. First, because it feared automation might cause unemployment, the government did not encourage the adoption of computerization in government and state-owned enterprises. Second, its interest in developing a domestic hardware industry led the government to impose extremely high tariffs (350 percent in much of the 1970s and early 1980s). Third, Indian private sector companies had little incentive to adopt information technology to improve operations and productivity, given the highly protected nature of the economy. Overall, this outward orientation stood in significant contrast to the orientation of much of the Indian manufacturing sectors which were focused on the Indian domestic market rather than the export market (Khanna and Palepu, 2004).

2.2. The Indian drug industry

Before the therapeutic revolution around 1940 there was no technology gap between Indian and foreign firms. Afterwards, foreign affiliates in India took advantage of local companies to expand their market share until 1970 when the Indian Patents Act was passed. It was obviously a turning point for the Indian pharmaceutical industry as it gave indigenous firms space to develop alternate processes, and they did so successfully. Therefore, these firms were able to keep prices low, introduce new drugs in the Indian market much earlier than before, and later on, in the 1990s, they started exporting to developed countries' markets. Undoubtedly, none of this would have been possible without the 1970 Act.

Furthermore, the chemical industry's relatively strong base for the whole Indian manufacturing sector was particularly critical for the development of a national drug industry inasmuch as the pharmaceutical industry was firmly chemical-based up to the biotechnology revolution.

By combining both aforementioned factors, indigenous generic companies gained strong competitiveness both at home and in foreign markets by successfully exporting their products. Those companies have currently embarked on a multi-faceted strategy of comprehensive internationalisation — i.e. direct investment, mergers and acquisitions, along with strategic alliances with large multinational companies.

2.3. The relationships with financial globalisation

So far, the bulk of the investments by Indian affiliates in Europe comes from parent firms because of the family-controlled nature of those companies and their reluctance to lose control over their affiliates. In some cases they used financial vehicles (ADRs or GDRs) but largely they had 'deep-pockets'. In a few cases, Indian investors have used more subtle financial tools to back their deals. Tata Tea was the first Indian company to resort to a leveraged buyout in 2000 to take over the British Tetley company. But in this prominent case the Indian company had no choice since Tetley had previously been acquired by equity funds.

3. Indian enterprises in Europe: why, when, where and how?

Corporate data generally give useful insights about companies' strategies, but due to the paucity and inconsistency of such information we had to collect data on the identity, patterns of entry and eventually partnerships by Indian enterprises in Europe. Therein, numerous sources have been used: national or local agencies supporting inward investment, professional associations, information brokers (India Advisory Partners, Thomson Financial) and corporate information such as annual reports.

Basically, two types of operations have been taken into account: first, new or *greenfield* investments in plants, development centres or commercial offices; second, M&As of/with European companies, and in some cases, U.S. affiliates. Very few expanding operations have been checked, and no divestiture or closing ones. We cannot therefore definitely ascertain whether Indian enterprises in Europe have

divested of company affiliates or even closed factories as firms are generally reluctant to give publicity to such events.

A first counting for the 1985/2005 period provides a fairly similar level of setting up operations and M&A deals (around 200).

An interesting finding is the large diversity of investors. Thus, we encounter large groups or conglomerates (Bharat Forge, Tata or Reliance), mid-sized enterprises (Avesthagen) or very specialized ones (Ranbaxy or Suzlon Energy). As far as internationalisation is concerned, we also get various actors: early movers (Tata Consulting Services or United Breweries), companies making rapid progress in their internationalization (Bharat Forge), or firms at their early stage (Jubilant Organosys or Subex). Note that these features are not exclusive.

Besides, the new investments are mostly service-oriented (more than 80 percent), while the manufacturing component is larger for takeover deals and equity acquisitions.

The mainstream international business literature advances five motivations or categories for enterprises to invest abroad: to acquire natural resources (mineral or foodstuffs), to tap technological knowledge and capabilities, to gain access to new markets, to seek diversification, and to capture strategic assets.

Although the distinction was not always clear-cut to place each investment case in one category, one motivation seems to be ahead for Indian companies — *i.e.* to improve their global market positions, which is part of the rapid growth of strategic asset-seeking FDI over the last two decades (Dunning 1998). Market-seeking investments are also prominent whereas technology-seeking investments, such as to tap proprietary technology, seem less important. Another specific factor, which can be labelled 'prestige factor', is driving the international expansion by Indian firms, particularly in mature markets through bids to acquire recognizable foreign brands.

An in-depth analysis of investment cases from Indian companies in Europe reveals five characteristics which are largely embedded in the institutional and economic context of the home country: first, a new phenomenon; second, a multi-dimensional entry pattern; third, the prevalence of family-controlled companies; fourth, an uneven spatial distribution; and lastly, a relatively narrow industry distribution.

3.1. A new phenomenon

As mentioned earlier, Indian FDI to developed countries has occurred recently. Even if Europe is still lagging behind the United States the inflows have been gaining momentum since 2002. Actually, the presence of Indian investors dates back to the 1970s when Tata Consultancy Services set up its first office in London in 1975.

Afterwards, acquisition deals were conducted by public enterprises (Burmah Oil) in oil refinery and the distribution sectors which were considered as strategic by Indian governments. This trend continued in the early 1990s when large Indian companies acquired state-owned enterprises from Central and Eastern Europe through tenders in those countries' privatization programmes. Indian companies then bought plants from the German *Treuhandanstalt* agency at very low cost after Germany's 1990 reunification. Indian companies such as Orkay, Usha Rectifier or Dalmia acquired manufacturing footholds in Europe in the textile, electronic and chemical sectors. Apart from the business opportunity, the entry of Indian companies into Europe had more to do with familiarity with East German in terms of management and tradition of government involvement in manufacturing activities than in true synergies between

both sides. This inclination is still alive: for example, Mahindra & Mahindra, India's largest tractor manufacturer, which also makes multi-purpose vehicles, made a bid to acquire a Romanian state-owned tractor maker in early 2006.

If along the 1990s, the entry of Indian investors into Europe through new business set-ups or M&As was relatively modest, the trend gathered pace in 2001 to accelerate in 2004, particularly for company creations.

3.2. A multi-dimensional entry pattern

An interesting finding about the investments by Indian companies in Europe is the simultaneousness of diverse forms of entry: direct investment, M&As, and increasingly strategic alliances with large foreign multinational companies. In this sense, Indian companies are not following the historic path previously taken by Western multinational companies which was more of a sequential path, but are clearly grasping the globalization age and its opportunities and constraints. We have already provided some insights into direct investment and M&As, so let's now briefly supply more details about strategic alliances with Indian companies as partners. Following seminal contributions by authors such as Kogut and Zander (1992), a growing body of literature in the management field has emphasized the crucial role played by alliances in knowledge-intensive industries. Various research studies have underlined the complementarity of the intangible assets controlled by each partner. As a result it is not surprising to find Indian companies as partners in such settings due to their strong competitive advantage particularly in software and IT services, and the drug industry. If Indian companies, on the one side, are keen to participate in those arrangements, on the other, Western companies are also eager to engage in cooperation with Indian companies in order to tap useful resources and capabilities.

3.3. The prevalence of family-controlled companies

As mentioned earlier, family-controlled or ethnic-controlled companies is still the rule for Indian companies. In fact, this is not specific to India as it is also prevalent in Asia with the exception, for historical reasons, of Japan and mainland China. Unsurprisingly, there are numerous Indian family-controlled companies in Europe. We found subsidiaries from groups controlled by old families such as Tata and Birla, along with companies controlled by new families — for example, Bharat Forge by the Kalyani family, and the Reliance group by the Ambanis. However, we also found non-family controlled firms more particularly in the software development and IT services industries such as Infosys and HCL. Those companies are generally managed by professionals. This is a marked difference with public companies — *i.e.* companies with an open capital structure which is the norm in Europe and of course in the United States — because there is no place for hostile bids. As a consequence, the Indian acquisitions in Europe involve cash compensation in order to restrain the issue of new shares or equity exchanges so as not to dissolve family control.

3.4. Spatial polarisation

At first glance, the spatial projection of Indian companies' investments across Europe is quite different from that observed at macro level using FDI data (on a balance of payments basis); even though the United-Kingdom ranks as the first European host

country in both cases. The UK is still a gateway to European markets: it provides a base for regional headquarters coordination and command activities (for example, TCS set up its regional headquarters in London in 1994 after first starting business there in 1975); and a springboard for the Indian companies willing to expand in Continental Europe. As for other countries, while France still ranks as the third most-favoured destination, there is a *chasse-croisé* between the Netherlands and Germany with the Netherlands ranking second for FDI flows and Germany holding the second place for the number of setting up operations and M&A deals. For Eastern European countries, the gap is more pronounced. These discrepancies can be explained by the use of a different computational base: FDI flows are computed in monetary value while setting up and M&A operations are the result of a mere arithmetic count. Therefore, there is no inconstancy between the two data sources: for example, the Netherlands' second rank is due to its fiscal attractiveness particularly for financial holdings, while Germany's second rank for the number of operations results from Germany's spatial centrality in an enlarged EU along with the density and diversity of German industry (Mittelstand). Germany is also the first target for the acquisition of drug companies by Indian counterparts (Table 1).

The 2004 EU enlargement to Hungary, Poland and the Czech Republic² is a new opportunity for the Indian enterprises willing to enter European markets or expand their presence. A crucial factor is the low wage levels of workers with the appropriate skills in the software development and IT services. As a result, these States are not in direct competition with Western countries for those activities, but increasingly so with India where software engineers' wages have increased over the past few years despite the fact that India produces over 300,000 new postgraduates every year. However, competition does not affect call centers which are still located in India or in other developing countries such as Bangladesh.

The industry specialisation of Indian investments implies quite specific spatial distribution across Europe as investments are mainly concentrated in densely populated areas which can supply the labour market with the many varied skills in demand. Clearly, these investors are trying to reap the benefits of agglomeration effects and scale economies. France's *Ile-de-France* region, the UK's greater London and Germany's Munich and Ruhr areas thus receive many more Indian inflows than other areas. In addition, as most surveys show, underlying factors such as cultural dynamism, access to an efficient educational system and efficient transport interconnectivity are all part of those areas' attractiveness (Veltz 1996).

3.5. *Narrow industry specialisation*

At the first blush, the array of Indian investments already made in Europe is relatively large. However, the bulk of them is still focused on highly skilled activities in two prominent sectors: first and foremost, software development and IT-enabled services; second, the pharmaceutical industry, more particularly the production and distribution of generics.

This twofold specialisation concerns *greenfield* investments which are very sizeable. In this case we can speak of mono-specialisation as over 65 percent of operations occur in the same field. In the case of software development and IT-enabled services Europe does not only attract the top five Indian enterprises (TCS, Infosys, Wipro,

² According to one ranking (A.T. Kearney 2004) the Czech Republic offers the most attractive conditions in Europe for the off-shoring of software and IT services.

Satyam and HCL) but also mid-sized ones. This huge presence is characterised by a scattering of representative or commercial offices, with still only a few development centres. Such layout is viewed as necessary by Indian companies so they can enlarge their European market share, strengthen their links with corporate customers or with their European counterparts with a view to forming strategic alliances which will put Indian firms in direct competition in the home markets of first-rank European companies such as Cap Gemini Ernst & Young or SAP. To a lesser extent, Indian enterprises also pursue the acquisition of small European firms so as to secure very specific assets. In 2005, for example, India's i-Flex Solutions acquired Login SA, a French company specialised in treasury management.

The pharmaceutical industry comes next, but this sector is way behind for company setting up operations while it is ahead for M&As. Here, Indian enterprises are large (Ranbaxy Laboratories), mid-sized (Wockhardt) or start-ups such as Strides Arcolab whose stellar growth is pulled by foreign markets.

Table 1 : Acquisitions of European pharmaceutical firms by Indian companies (2000-2006)

Date	Target company	Target Company's Country of origin	Buyer
2000	Bayer-Generics Pharmaceutical	Germany	Ranbaxy Labs
2001	German Remedies	Germany	Zydus Cadila
2003	CP Pharmaceuticals	UK	Wockhardt
2003	RPG Aventis	France	Ranbaxy Labs
2003	Alpharma France (Alpharma/ USA)	France	Zydus Cadila
2004	Esparma	Germany	Wockhardt
2004	Pharmaceutical Services	Belgium	Jubilant Organosys
2004	Temmler Pharma	Germany	Wockhardt
2005	Docpharma	Belgium	Matrix Labs
2005	Heumann Pharma	Germany	Torrent Pharmaceuticals
2005	Betapharm	Italy	Strides Arcolab
2005	Polish Sterile	Poland	Strides Arcolab
2005	Efarmes	Spain	Ranbaxy Labs
2005	ICN (Valeant Drugs Pharmaceuticals/ R-U)	Hungary	Sun Pharmaceuticals
2006	Explora Labs	Switzerland	Matrix Labs
2006	Betapharm	Germany	Dr Reddys Labs
2006	Terapia	Romania	Ranbaxy Labs
2006	Ethimed	Belgium	Ranbaxy Labs
2006	Allen (GlaxoSmithKline/ R-U)	Italy	Ranbaxy Labs

Source: SDC Platinum database

The drug industry's above specialization is even more reinforced if one takes the value of M&A deals into account. As a matter of fact, the largest operation by Indian enterprises in Europe concerns the pharmaceutical industry with the acquisition by Dr Reddys Laboratories of Germany's fourth-largest generic drugmaker Betapharm

Arzneimittel for 410 million euros in 2006. It was not a single operation but part of a swelling wave of European companies and foreign affiliates' acquisitions that started in 2003 (**Table 1**). Several reasons can explain this trend. First, there is a structural explanation which has much to do with the high barriers to entry into this industry — increasing R&D costs for a new molecule together with stricter requirements for clinical tests. The second reason is of a contingent nature and can be best described as the opening of an opportunity window — namely European governments' health cost reduction policies, the end of patents on important drugs, and the refocusing induced by the European pharmaceutical companies and U.S. subsidiaries' desire to capture the more substantial gains yielded by new molecules in some specific domains (cardiovascular and anti-infectious). Germany's prominent place (between 2000 and 2006, 6 out of 19 deals targeted German companies) is due to its market share: it is the largest European market for branded generics — Wockhardt's sales, for example, make up 40 percent of that market. The third reason concerns the threat to Indian companies' own home market from the world's pharmaceutical giants, which have more reason to expand in India now that the country has adopted the WTO patent law ³.

All of the above factors have offered attractive opportunities to the Indian companies willing to enter the European markets. When the amounts required were not too high (which can occur in the case of an overbid), this option provided the chance to have full advantage of well-known brands with their marketing settings and commercial networks, and thereby become immediately operational in European markets. In short, the main determinant of M&A activity in the drug industry was rapid access to large geographic markets.

Automotive equipment manufacturing comes third for M&A deals, behind the drug and software industries. This ranking was bolstered by the acquisitions of mid-sized European companies by large Indian enterprises (Tata Motors or Mahindra & Mahindra) or more specialised ones (Amtek Auto, Bharat Forge, EL Forge or Sundaram Fasteners). In so acting, Indian enterprises managed to get immediate access to vital technologies or manufacturing bases in Europe, and thus become part of regional automotive subcontracting networks. They were consequently given both direct access to one of the three global bases for innovation and production in the automotive industry and the opportunity to widen their customer base.

So, to sum up, the examination of M&A operations shows that industry distribution is larger than that of creations. Apart from the software, drug and automotive industries there are still numerous operations in such sectors as chemicals, metal products, and food. Some operations are obviously part of strategies aiming to make already large Indian companies into worldwide firms: for example, in 2004, Reliance Industries acquired a German polyester producer and consequently became the world's largest polyester producer. Other Indian companies target more specific assets as illustrated by Jindal Polyester's 2003 acquisition of the French REXOR — a Rhône Poulenc ex-affiliate previously acquired by its managers and an equity fund through a management buyout — because REXOR had specific know-how in the polyester field.

Finally, after studying all of these acquisitions, it becomes possible to establish the recurrence of operations by some large Indian enterprises — either successive holdings acquisitions so as to secure a majority interest or new acquisitions.

³ By recognizing product patents, India accepts that generic drugs cannot be sold in India until the patents on branded drugs have expired.

All in all, the motivation for current Indian foreign investments is economic efficiency and profitability criteria (pull factors), rather than the desire to escape a restrictive business home environment (push factors), as used to be the case before economic reforms were introduced in India. We can also go back to another seemingly paradoxical finding: Indian FDI in Europe is mainly horizontal — *i.e.* FDI undertaken for market considerations. According to theory, a fall in trading costs does not bring about any FDI increase, more especially in the case of horizontal FDI. This reasoning implies that lower trading costs, *ceteris paribus*, make it more profitable for firms to serve foreign markets via exports rather than sell their production directly in the foreign markets. Yet, this statement is not valid in our context: first, for software development and IT services face-to-face interaction is still required, hence scattering investments are made in offices across Europe⁴; second, as regards drug companies, support investments such as trade-related, and legal or administrative investments are equally important.

4. The impact on European economies

It is now common place that Europe is confronted with two structural challenges: first, chronic high unemployment and second, a low growth path requiring innovation. In this perspective, the effect of Indian investments in Europe seems fairly neutral since those investments concern mostly services such as marketing and commercial representations in high value-added sectors, even though in some areas, notably Eastern Europe, the large IT-enabled services development centres have had some impact. Furthermore, as the acquisitions by Indian investors are part of a strategy to assume global leadership rather than make synergy gains through manufacturing downsizing or a quick profit by financial stripping, they do not cause disruptive effects on employment and consequently on local communities.

Notwithstanding the employment figures, the skills problem is worth being addressed. To do so, we need to go back to the innovation issue as Indian investors in Europe have flocked to high-tech sectors. Here, the impact could be more significant, even if it is not easy to gauge the results. Obviously, the arrival of numerous Indian software companies in Europe increased the demand for ICT skills; new practices and professional experience may affect the manpower structure. Besides, proximity with customers favours knowledge sharing, which may in turn enhance the competitiveness of European companies generally lagging behind the US for software outsourcing and off-shoring. Likewise, productivity gains could be reaped at macro-economic level since services are more pervasive in their effects than manufacturing. Another potential beneficial effect of Indian investors' presence in Europe's software or generic drug industries is an increase in competition (pricing pressures) which may subsequently entail some welfare impact for European consumers through lower prices.

Yet, there are some drawbacks too. If one considers European trade balances, the impact is negative because the competitiveness of Indian companies in Europe lies in the synergy of European distribution networks and Indian low-cost manufacturing facilities. It is not accidental if Indian national accounts have shown stellar growth in

⁴ In addition, MNC customers expect some presence or support in many countries, and often prefer dealing with a single global contact in only one outsourcing company to entering into multiple contracts with a whole range of local suppliers around the globe.

ICT services since 2002. As for the future the prospects are not too promising for the European manufacturing base because Indian companies can use other more competitive manufacturing places in Europe's neighbouring countries or elsewhere in Asia.

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