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FDI and Globalization in India

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Abstract

The Indian economy opened up in 1991 within the framework of liberal economic reforms. FDI inflows were stimulated in industry and services, so benefiting from the many comparative advantages of the country (human resources, emerging market). In 2004, FDI inflows officially amounted to $ 5.3 billion. They mainly came from the United States and Mauritius and concerned industrial sectors.

In parallel, some Indian firms started to grow in importance and to invest abroad: they had the financial means, experience, and ambition to acquire international recognition and they were encouraged by the Indian government. FDI issued by Indian firms amounted to more than $2 billion in 2004; it was principally addressed to developing countries and to Russia, however the share of industrialised countries was on the rise, and manufacturing and non financial sectors accounted for the bulk of it.

Introduction

This paper focuses on FDI (foreign direct investment) as a vector of Indian globalization. Recently, not only did India become a more frequent destination for FDI, but also, many Indian firms started to invest abroad on a very large scale with, sometimes, some stunning takeovers in industrialised countries. The reforms undertaken since 1991 in India have unleashed the potential growth of the economy and stimulated international trade, outsourcing and FDI. Changes have been so many that investors have started to take a fresh look at India. At the same time, some Indian firms have become global players.

1 – India: a latecomer to FDI

India's share in world FDI is minor, notably when considering its size. Indeed, the opening of the

country is relatively new and the history of its FDI on a large scale very short.

1-1 Low amounts of FDI

At first sight, India appears to be an "underperformer" as far as FDI is concerned. In India, as in most developing countries, inward and outward FDI are not easy to analyse because they are generally low and fluctuating. Data relating to FDI inflows (and probably to outflows as well) are underestimated because of their national definition and interpretation. The Reserve Bank of India (RBI) and the Secretariat for Industrial Assistance (SIA) which officially publish statistics have, since 1991, only reported the equity component of FDI. So, reinvested earnings[1] have not been taken into consideration while IMF[2] guidelines estimate they are part of FDI inflows. Indian data include neither the proceeds of foreign equity listings nor foreign subordinated loans to domestic subsidiaries. Overseas commercial borrowings are also disregarded, as well as some depository receipts over 10 per cent of the equity coming from foreign institutional investors (Srivastava, 2003). So, there is a lot of scope for improving India's FDI statistics in order to put them in line with international standards.

Officially, at the end of 2004, India's stocks of inward FDI amounted to $38.7 bn, that is, only 0.4% of world stocks, and 1.7% of investments received by developing countries. These stocks represented 5.9% of Gross Domestic Product (GDP) in 2004, a very small ratio compared with developing countries average (26.4%). We notice however that Indian stocks were 23 times greater in 2004 than in 1990. In 2004, India held the15th slot in terms of inward FDI stock among developing economies (WIR, 2005).

Table 1 - FDI inward stock

($ billion)

	1990	2000	2004
World	1769	5781	8895
Developing Economies	364	1734	2226
India	1.7	17.5	38.7

Source: WIR, several years

If the Indian position in world outward FDI is not very high, it has increased rapidly since 2000. At the end of 2004, India issued $6 bn of FDI. Indian stocks amounted to 1% of GDP in 2004, far from the average observed in developing countries (12.7%).

Table 2 - FDI outward stock ($ billion)

($ billion)

	1990	2000	2004
World	1785	6148	9732
Developing Economies	147	869	1036
India	0.1	1.9	6.6

[1] That is, the part of foreign investor profits that are not distributed to shareholders as dividends and reinvested in the affiliates in the host country

[2] International Monetary Fund

Source: WIR, several years

Though Indian outward FDI was very low, growth has been very impressive, notably since 2000. In 2004, India held the 16th slot in terms of outward FDI stock among developing economies (and the 12th if we exclude tax havens such as Virgin Islands, Cayman Islands, Panama, and Bermuda) (WIR, 2005).

1-2 FDI is gathering momentum

The analysis of FDI inflows and outflows corroborates the trends previously observed as to their weakness, but it also points out the boom of Indian investments abroad since 2000. FDI received by India is quite recent: 42.4% of it has been carried out since 2001, with a year on year increase of 26.5 % in 2003 and of 23.3% in 2004. In 2004, FDI reached a record level of $5.3 bn, and India held the 7th rank among developing countries to attract foreign investors (behind China, Hong Kong, Brazil, Mexico, Singapore, South Korea, and Chile).

Though the share of world investment received by India remains weak (0.6% on average over the period 1992-1997, 0.7% in 2003 and 0.8% in 2004), it is increasing. Furthermore, if we take account of distortions of data formerly mentioned, actual FDI is higher than officially assessed. If we only add reinvested earnings by foreign firms, FDI inflows have to be increased by about 1.8 billion dollars in 2003 and in 2004. So, India would have received about 7 billion dollars of FDI in 2004.

Table 3 - FDI inflows

($ billion)

	1992-97*	1998	1999	2000	2001	2002	2003	2004
World	310.9	690.9	1086.7	1387.9	817.6	*716.1*	*632.6*	*648.1*
Developing economies	118.6	194.0	231.9	252.4	219.7	155.5	166.3	233.2
India	1.7	2.6	2.2	2.3	3.4	*3.4*	*4.3*	*5.3*

*Annual average.
Source: WIR 2004 and others

The growing trend in FDI inflows is also pushed by greenfield investments. The amount of Greenfield FDI has risen by 82.8% in 2003 with 457 projects, and by 50% in 2004 with 685 projects (WIR, 2005). As for the M&As by foreign firms, they amounted to 949 million dollars in 2003 and to 1760 million dollars in 2004 (WIR, 2005).

Table 4 - Cross-border Mergers & Acquisitions in India,

($ million)

Year	1997	1998	1999	2000	2001	2002	2003	2004
Sales	1.520	361	1.044	1.219	1.037	1.698	949	1.760

Source: WIR 2004 and 2005

Data available for 2005 lets us suppose that FDI received by India is on an ascendant trend: it increased by 35% over the period April-October 2005, thus approaching the target of 7.5 billion

dollars in 2005-06, set by Mr Kamal Nath Commerce Minister[3] (IBEF, Feb 2006).

Table 5 - FDI flows as a percentage of GFCF in 2004

	Inward	Outward
India	3,3%	1,4%
China	8,2%	0,2%
Developing countries	10,5%	4,2%

Source: WIR 2005

Indian FDI outflows surged to 2.2 billion dollars in 2004; it was a record level. Indeed, if it represents only 0.3% of world FDI outflows and 2.6% of outflows issued by developing countries, the progression of Indian investments has been really spectacular since 2002 when they reached 1.1 billion dollars, while they amounted to around 100 million dollars during the previous years.

Table 6 -FDI outflows
($ billion)

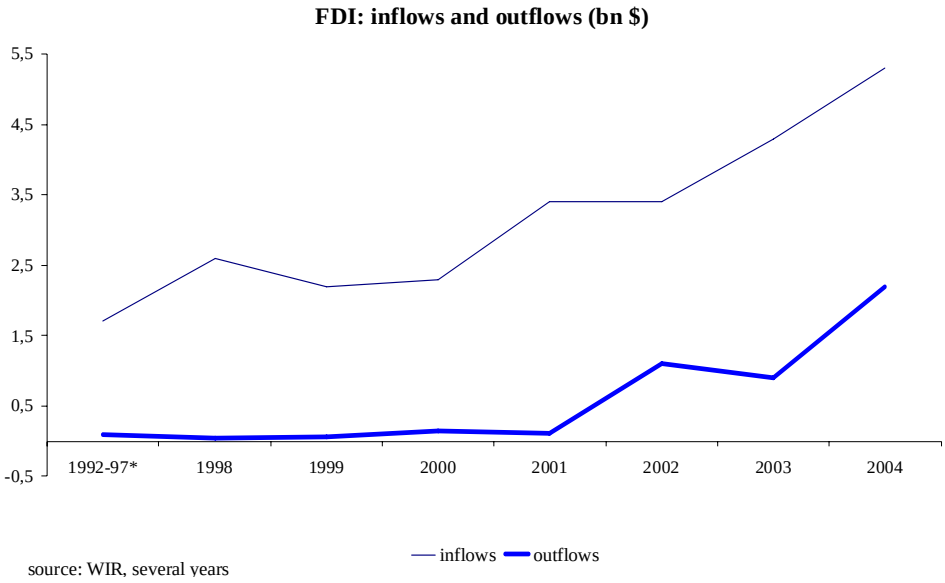
	1992-97*	1998	1999	2000	2001	2002	2003	2004
world	3238.2	687.2	1092.2	1186.8	721.5	652.2	616.9	730.2
Developing economies	51.3	53.4	75.5	98.9	59.8	47.8	29.0	83.2
India	0.09	0.04	0.07	0.15	0.12	1.1	0.9	2.2

*Annual average
Source: WIR 2004 and others

Indian FDI outflows issued in 2002, 2003, and 2004 represented two thirds of Indian stocks of FDI at the end of 2004. In 2004, Indian FDI outflows amounted to 1.4% of the Gross Fixed Capital Formation: it was less that the average in developing countries (4.2%), but more than the ratio prevailing in a country such as China (0.2%). In 2004, India held the 7th rank among developing countries for its investments in foreign countries (behind Hong Kong, Singapore, Brazil, Taiwan, South Korea and Mexico). It is particularly interesting to put in parallel the evolution of Indian FDI inflows and outflows.

[3] With auto and mining sectors expected to attract huge funds.

Chart 1



source: WIR, several years

India received 5.3 billion dollars of FDI in 2004, but it issued 2.2 billion dollars of FDI abroad: so the later represented 41.5% of the former. This is quite an astonishing result, as in developing countries FDI outflows are generally very low. That shows that Indian firms are going global very rapidly. Furthermore, it is very likely that FDI outflows are underestimated (UNCTAD, 2005), either for fiscal reasons, or because the Indian firms investing abroad under declare the amounts they invest.

1-3 India was kept out of world FDI until 2000 but it is becoming a global player

Several reasons can explain the "weakness" of inward and outward FDI registered until recently. Being a developing country with very low GDP per capita, many illiterate people and poor infrastructures, India could not attract FDI. On the one hand, developing countries only attract foreign investors when they own raw materials or natural resources, but that was not the case with India. On the other hand, Indian firms stayed confined in their country to do business because they had neither opportunities nor financial and technical means to invest abroad and because such operations were not really well regarded by the government.

Furthermore, India implemented after its independence (1947), an inward looking strategy including planning, nationalizations, an import substitution policy, where tax structure was complex and FDI conditionally tolerated (for internal needs and with minority shares). Indeed, some industrial partnerships were historically concluded between Indian firms and TNCs: Tata and Daimler Benz in the 1950's, Bajaj and Piaggio (Vespa) in 1960 and Kawasaki in 1983; also Mahindra formerly collaborated with International Harvester and American Motors, Modi with Continental and Xerox, … However Coca Cola and IBM were expelled from India by Indira Gandhi in 1973, because they did not want to reduce their ownership stake to 40%. The success of the first JV established in 1984 between an Indian and a foreign firm (Maruti and Suzuki) was not really welcome, even if it is now considered a great success.

If some measures of de-licensing were taken in 1985 and 1986 by Rajiv Gandhi, it is mainly in 1991 that Indian opening to foreign investment occurred, in parallel with the liberalization of the economy. Private and foreign firms were permitted to invest in activities previously reserved for the public sector. FDI was allowed not only for the domestic market but also for exports; investment ceilings where raised, policy environment and procedures were significantly simplified and streamlined[4], and FDI abroad by Indian firms became also conditionally possible. That was finally beneficial to the Indian economy which started to emerge progressively, with, however, inertia.

Liberalising has been combined with world globalisation, thus benefiting from the international context of deregulation, lower transport costs and rapid expansion of internet. Growing international labour division and the fragmentation of TNCs also proved beneficial. Since 2000, India has kept pace with some of the more conspicuous developing countries, such as the Asian Dragons, Brazil and China. India is a more and more active partner in regional arrangements and agreements such as ASEAN[5], Gulf Cooperation Council, BIMSTEC[6], South Asia Free Trade Area, Indian Ocean Rim Association for Regional Cooperation, SAARC[7] … In addition, India has signed, since 2000, many bilateral investment and trade agreements as well as double taxation treaties with an increasing number of countries (notably with other developing countries, but not exclusively): that stimulated exports and investments, all the more because, in parallel, the opening of the country was confirmed (elimination of many quotas, reduction of customs duties[8]).

FDI is nowadays perceived by the Government as a way to stimulate development, growth, and to create new resources. FDI is freely allowed in many sectors[9] with automatic approval[10], freedom of location and choice of technology. Imports and exports, repatriation of profits, dividends, and capital are also free[11]. On top of that, intellectual property rights are guaranteed.

Since November 2005, FDI is allowed up to 100% in most activities under the automatic route[12]. The Government also aims to attract foreign investments by setting up special economic zones[13], science parks and free trade and warehousing zones[14]. The Indian Investment Commission is charged with the responsibility of wooing investors[15]. Foreign investment is particularly sought after in power generation, telecommunications, ports, roads, petroleum exploration/processing,

[4] Until 1992, all foreign investments in India and the repatriation of foreign capital required prior approval of the government, and the Foreign-Exchange Regulation Act rarely allowed foreign majority holdings.
[5] Cambodia, Laos, Malaysia, Philippines, Singapore, Thailand, Vietnam, Myanmar
[6] Including since 1997, Bangladesh-India-Myanmar-Sri Lanka-Thailand Economic Cooperation, and Bhutan and Nepal since 2004
[7] South Asian Association for Regional Cooperation
[8] Such a trend was besides reinforced by the end of the textiles and clothing quotas (UNCTAD 2005).

[9] Sectoral ceilings remain in some activities.
[10] Initially, FDI's approval relied on matching exports and dividend repatriation. In July 1991, this approval became automatic in thirty-four industries designated high priority, up to an equity limit of 51 percent.
[11] Recently, foreign-equity ceilings in aviation services, private banks, non-news print publications and the petroleum industry have been adjusted.
[12] That is, without any prior approval.
[13] For instance, export oriented units and units in export processing zones benefit of tax holiday (100 per cent) for five years.
[14] In free trade warehousing zones, FDI are permitted up to 100%.
[15] Also, the Foreign Investment Promotion Board is a one-stop service centre and facilitator for FDI.

and mining. A ten-year tax holiday is offered to companies engaged exclusively in scientific R&D with commercial applications. On the other side, FDI by Indian firms abroad is more and more encouraged and perceived as a way to enhance the competitiveness of firms and to assert the power of India around the world.

Foreign trade also increased, although its share in world exports remains low: 0.8% for merchandise exports (rank 30) and 1.7% for services trade in 2004 (rank 16). In 2004, exports grew by 30% for merchandises to reach $75.5 bn[16] and by about 70 % for commercial services to reach $39.5bn (WTO, 2005): software and IT-enabled services came with such a growth.

Since the end of the 1990's, the dynamism of services and high tech sectors have contributed to modernize the Indian economy and to boost international trade and investments. Policies implemented have been decisive to support information and communication technology industries, as well as the pharmaceutical and biotechnologies sectors. Leading IT firms shaped in the 1980's (such as Tata Consulting Services, Wipro, Infosys), benefited from a fiscal advantages, and a favourable environment thanks to the creation of Public Research Centres (in Army, in Telecommunications) and of software technologic parks. The role played by the NASSCOM (National Association of Software and Service Companies) since 1988 acting as a catalyst to the growth of the IT industry is worth being mentioned. It contributed to facilitate trade and business in software and services, and to encourage research and education in India. NASSCOM acted simultaneously as an advisor, a consultant and coordinating body, with representatives on various committees in the Government of India[17].

So doing, India became well known all around the world for its services and software activities. Between the beginning of the 1990's and 2005, computing and information technology services registered an annual growth rate of 8-9%. In 2005, it accounted for 5% of Indian GDP. Such dynamism created hundreds of thousands of jobs and given self-confidence to a new generation of industrialists and entrepreneurs to compete globally. It also attracted many MNCs which started to outsource their business process in India.

If some Indian companies established partnerships with foreign firms as early as the middle of the 20th century, the bulk of them go back to 10 years ago, with the booming of FDI, JV, subcontracting, outsourcing (software, call centres, financial services, …)[18] which contributed to modernize productions facilities, to promote significant technology transfers and to improve performance. Indian research was stimulated[19], thus creating local demand for new services and high technology industries[20] (WIR, 2005).

[16] Gems and jewellery, engineering goods, petroleum products, ores & minerals, and chemicals and related products were the key drivers of India exports.

[17] In December 2005, the NASSCOM included 950 members (Among them, 150 are global companies from the US, UK, EU, Japan and China) accounting for over 95 percent of the revenues of the software industry in India.

[18] It has been estimated that as soon as 2000, 160 enterprises among the Global 500 had externalised their IT services and that in 2005 they were almost 400 (Boillot, 2005)

[19] For instance, Indian pharmaceutical companies such as Dr. Reddy Laboratories and Ranbaxy have R&D alliances with Novo Nordisk, Novartis and GlaxoSmithKline.

[20] Texas Instruments, the first TNC to be allowed to establish a wholly owned software affiliate in India in 1986 not only inspired other TNCs to set up operations in the country but also spurred the growth of the indigenous software and business services industry (WIR 2005). In many ways, foreign investors have opened new job opportunities for Indian researchers in the interface between science and business.

In parallel, foreign firms gave to Indian companies an opportunity to meet with international levels and production standards (quality and safety) and to acquire new capabilities. Indian firms also had the opportunity to get information about foreign markets. Lastly, these relations prompted competition in local markets where Indian firms used to operate, until 1991, in a protectionist context. Progressively, some of them were able to become formidable international competitors[21].

India has a well-established major manufacturing sector that spans almost all areas of activity. Despite revolutionary changes in the business environment, many old family groups have remained at the forefront and maintained their hold over their companies with dexterity. Their successors are more and more well-educated and well-versed in the art of management; most of them generally studied in the USA, in the United Kingdom, or in other European countries. The capitalist culture of enterprises such as Tata, Birla Kirloskar, Mittal, Mahindra, Mafatlal, Walchand, Mahindra, Bajaj, Singhania, is deeply rooted. It is interesting to notice that besides these old and prosperous family groups, many other renowned Indian companies have been created in the last few decades: for instance in the case of Ranbaxy incorporated in 1977, of Dr Reddy's (1984), of Videocon (1988), of Wipro, created in 1945 but which started to work in information technology in 1982 (for the Indian market first). Also, some Indian firms are true start-ups recently incorporated, and, in some regards, global born: they often operate in the field of the new technologies, that is the case of Infosys, of Moser Baer, KPIT, Satyam, HCL Technologies, … All these firms have technical skills and required capabilities to act on a global level.

2 - Who invests in India and why?

2-1 The United States is the first investor

Most of FDI inflows come from a few countries. Between 1991 and 2005, investments of 10 countries accounted for 71 percent of FDI, the main investor countries being the USA, the Netherlands, Japan, and the United Kingdom.

[21] For instance, Videocon conquered the opportunity to buy a branch of Thomson TV thanks to a former production agreement with Matsushita.

Table 7 - Top investing countries in India, according to FDI inflows 1991-2005 *($ billion)*

Country	**Aug. 1991-March 2002**	**2002-03**	**2003-04**	**2004-05**	**2005-06**	***Cumulative inflows Aug1991-Nov 2005***
Mauritius	6.632	0.788	0.567	1.127	1.760	*10.874*
USA	3.188	0.319	0.360	0.668	0.356	*4.891*
Netherlands	0.986	0.176	0.489	0.267	0.068	*1.986*
Japan	1.299	0.412	0.078	0.126	0.098	*2.013*
U.Kingdom	1.106	0.340	0.167	0.101	0.196	*1.91*
Germany	0.908	0.144	0.081	0.145	0.052	*1.33*
Singapore	0.515	0.038	0.037	0.184	0.164	*0.938*
France	0.492	0.112	0.038	0.117	0.008	*0.767*
Sth Korea	0.594	0.039	0.024	0.035	0.057	*0.749*
Switzerland	0.325	0.093	0.045	0.077	0.064	*0.604*
Total FDI Inflows	***23.829***	***3.134***	***2.634***	***3.754***	***3.348***	***36.704***

Source: RBI (Reserve Bank of India), 2006 February

According to data relating to the period 1991-2005, Mauritius is the biggest source of "foreign" direct investment. But even if India and Mauritius have close political links and close bilateral relations rooted in common kinship, culture and interests (about 70 percent of the population of Mauritius is of Indian origin), data are biased. Mauritius has low rates of taxation and an agreement with India on double tax avoidance regime. For these reasons, some multinationals set up companies in Mauritius before going to India. Investments from Mauritius in India are operated by Indian firms, either public[22] or private[23].

Apart from Mauritius, the United States is the first investor in India: it contributed about 13 percent of total inward FDI between 1991 and 2005. Both countries have close relations: the United States is the largest trading partner of India[24] and a broad Indian community lives in it.

[22] For instance, it is the case of : Life Insurance Corporation, New India Assurance, State bank of India International, Bank of Baroda, Indian Oil Corporation, and so on.

[23] It is the case, notably, of Infosys, Ajanta pharma, Apollo Tyres, Pentafour, Arvind Mills, Ashok Leyland, and so on.

[24] In 2004, principal US exports were diagnostic or lab reagents, aircraft and parts, advanced machinery, cotton, fertilizers, ferrous waste/scrap metal, and computer hardware. As to major US imports from India, they included textiles and ready-made garments, Internet-enabled services, agricultural and related products, gems and jewellery, leather products, and chemicals. Bilateral trade in 2004 was 21.7 billion of dollars.

Far behind the USA, Japan (5.5% of FDI inflows received by India), Netherlands (5.4%), United Kingdom (5.2%) are significant investors. Germany follows (3.6%), then Singapore (2.6%), France (2.1%), South Korea and Switzerland. The European Union's FDI in India is higher than that from the US. FDI from Netherlands, United Kingdom, Germany, and France, registered between 1991 and 2005 accounts for 16.3% of the total. In 2004-2005, Mauritius has still again been the main investor with 30% of total inward FDI, followed by United States (17.8%), then by Netherlands (7.1%), Singapore and Germany.

2-2 Manufacturing sectors attract the highest FDI inflows

Between 1991 and 2005, FDI received by India was mainly related to manufacturing, notably sectors such as electrical equipment (including computer software and electronics) which received 22.5% of FDI inflows, transportation industry (14.4%), telecommunications (13.2%), fuels (11.6%), and chemicals (8.7%). Services accounted for 13.4%. In recent years, some sectors such as electrical equipment, services, drugs and pharmaceuticals, cement and gypsum products, metallurgical industries have had the wind behind them insofar as more than the half of FDI regarding them was made after 2002, compared to an average of 39.4% for all sectors.

Table 8 - Sectors attracting highest FDI inflows (1991-2005)
($ billion)

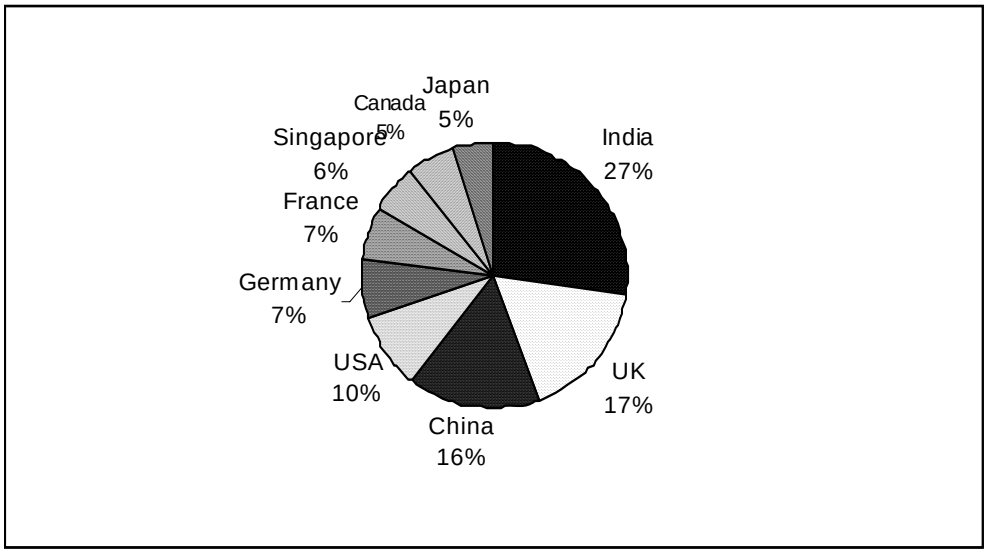
Sectors	Cumulative FDI Inflows 1991-2005	Cumulative FDI Inflows 2002-2005
Electrical equipement	4,862	2,734
Transportation Industry	3,124	1,110
Services	2,908	1,462
Telecommunications	2,863	0,624
Fuels (power, oil refinery)	2,514	0,416
Chemicals (other than fertilizers)	1,887	0,538
Food processing industry	1,173	0,222
Drugs and pharmaceuticals	0,946	0,552
Cement and gypsum products	0,746	0,483
Metallurgical Industries	0,624	0,393

Source: Reserve Bank of India

Since 2002, services hold the second rank in attracting FDI. Business services (IT, software, financing, insurance, real estate, etc) are gathering momentum, in parallel with the "tradability revolution" in services in the world. India is the main destination for off-shoring of most services

as back-office processes, customer interaction and technical support, R&D[25] (WIR, 2005). Indian services are more and more sophisticated with higher price tags (reading medical X-rays, analyzing equities, processing insurance claims). According to data provided by OCO Consulting (2005), India is, by far, the country which attracted the greatest number of projects in IT and software. Since 2002, of 1913 projects observed, it attracted 519[26], that is, 27%[27].

Chart 2: It & Software: Top locations by number of projects, Jan 2002- Aug 2005



Source: OCO Consulting (2005)

2-3 The developed states of the Indian Union attract the largest part of FDI

Foreign firms choose to locate their activities in the most developed areas of the country and, if possible, in poles of competitiveness when they exist.

[25] Among them, we find, abstracting and indexing, call centres data entry and processing, electronic publishing, mailing list management, secretarial services, technical writing, telemarketing, web-site design, interpretation of medical scans, flight reservations, and so on (WIR, 2004).

[26] Among them we find notably investments by Microsoft, Oracle, Syntel, SAP and Cybernet Software Systems

[27] However, during the same period, China seems to have attracted the largest ones in terms of job creation, with Satyam Computer Services and Bell Net each adding 3000 jobs

Table 9 - FDI inflows according to areas from 2000 to 2005

Regional Office and State covered by FDI	%
New Delhi (Delhi, part of Uttar Pradesh and Haryana)	25.9
Mumbai (Maharashtra, Dadra and Nagar Haveli, Daman & Diu)	21.2
Bangalore (Karnataka)	7.6
Chennai (Tamil Nadu & Pondicherry)	6.0
Ahmenabad (Gujarat)	3.3
Hyderabad (Andhra Pradesh)	3.2
Chandigarh (Punjab,Haryana, Himachal, Pradesh)	1.6
Kolkata (West Bengal, Sikkim, Andaman & Nicobar Islnds	1.3
Panaji (Goa)	0.6
Kochi (Kerla, Lakshadweep)	0.4
Bhubaneshwar (Orissa)	0.3
Bhopal (Madhya, Pradesh, Chattisgarh)	0.2
Guwhati (Assam, Arunachal, Pradesh, Manipur, Meghalaya, Mizoram, Nagaland, Tripura)	0.05
Jaipur (Rajasthan)	0.02
Patna (Bihar, Jharkhand)	0
Kanpur (Uttar Pradesh, Uttranchal)	0

Source: Regional Offices of RBI

Eight Regional Offices received more than 70% of Indian FDI inflows[28]. New Delhi and Mumbai and their surroundings include almost the half of FDI received by India since 2000, with respectively 26% and 21% each. Far behind, are the areas of Bangalore and Chennai (with respectively 7.6% and 6% of FDI inflows), then places surrounding Ahmenabad and Hyderhabad (about 3% each). All the previously mentioned areas include the main diploma-granting technical institutions and the most of diplomas awarded by private training Indian institutions.

It also appears that some areas are specialised. For instance, most software companies are in Mumbai and Bangalore[29], where Indian industry originally developed; but they are also

[28] Previous data have been reported by 16 Regional Offices of RBI as related to FDI received by them from January 2000 to November 2005. They concern amount of FDI of about $20 bn. However, states have not been identified for 28% of FDI received.

[29] Previous data have been reported by 16 Regional Offices of RBI as related to FDI received by them from January 2000 to November 2005. They concern global amount of FDI of about 20 billion of dollars. However, for 28% of FDI received, states have not been indicated officially.

developing quickly in Delhi and its surroundings as well as in Andhra Pradesh and Tamil Nadu. As to the main poles of competitiveness, they are mainly concentrated in the South on the axis Madras-Bangalore, and in the area of Delhi (Gurgaon, Noida).

2-4 Indian comparative advantages

India is becoming an attractive location for global business on account to its buoyant economy, its increasing consumption market, and its needs in infrastructure and in the engineering sector. To date, India is becoming a favourite destination for foreign enterprises. According to experts and TNCs managers, it is just ranked behind China and behind or on equal terms with USA (WIR, 2005)[30]; this trend was again recently confirmed by AT Kearney's FDI Confidence Index[31] (IBEF, 2006). TNCs invest in India to improve competitiveness and profits by means of cutting costs and to take a step in the Indian market. India has many comparative advantages for TNCs.

Though low literacy and education rates could suggest that labour is not skilled enough, it is not the case when human resources are normalized by the population size. Indeed, Indian skills in research, product design, and customisation of services are acknowledged. India is one of the largest pools of scientists, engineers, technicians in the world, more particularly in information technology, with competitive wage levels when compared to those of industrial countries[32] and the use of English in business and in technical and managerial education.

The contribution of Indians of the Diaspora to human resources is noteworthy. Until the end of the 1990's, this Diaspora was still rather resented for its success abroad; but it is no more the case. The government sees it as a potential source of skills, of entrepreneurship, of knowledge and of capital. It is even creating conducive conditions to favour its return: the idea is to turn the original "brain drain" into "brain gain"[33]. As a result, more and more Indians expatriated in industrial countries (mainly in United States and United Kingdom) start to come back to work in foreign affiliates or local companies; some of them creating their own business[34]. Furthermore, these last years, qualified workers went less abroad, seeing their country as a land of opportunity.

In the 1980's, some foreign companies such as Texas Instruments (semiconductor design) and Astra-Zeneca biopharmaceuticals were pioneers in research activities in India. They were followed in the 1990s by groups such as Motorola (telecommunications software), Microsoft (computer operating systems), ST Microelectronics (semiconductor design), Daimler-Benz (avionics systems), and Pfizer (biometrics). Nowadays, more than 100 TNCs[35] run research

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[29] Today, in Bangalore, there are apparently more data-processing engineers than in Silicon Valley.

[30] In the responses from experts, China is the favourite destination (85%), followed by United States (55%) and India (42%). In the responses from TNCs, China comes first (87%), followed by India (51%) and USA (51%).

[31] This index tracks investor confidence among global executives to determine their order of preferences

[32] India includes about 3 million of scientists and engineers, and 360000 engineering graduates per year.

[33] There was a time when nearly top 70 percent of the IIT (Indian Institute of Technology) pass-outs were going abroad, but the latest data shows that the percentage is down to 30 percent.

[34] In Bangalore, for example, some 35,000 non-resident Indians have lately returned with training and work experience from the United States (WIR, 2005).

[35] For instance, we can quote General Electric, Intel, Cisco, Hewlett-Packard, IBM, Lucent, Boeing, ZTE, Huawei (China) , Flextronics (Singapore), or pharmaceutical companies such as Eli Lilly, Glaxo SmithKline, Novartis, Sanofi-Aventis.

activities in India and their number is growing fast.

The availability of qualified workers, the existence of internationally reputed R&D institutes (Indian Institute of Technology, Indian Institute of Science, Indian Institute of Chemical Technologies, Centre for Drug Research), and the emergence of many Indian firms as service providers or as partners[36] contributed to attract TNCs in India to perform R&D.

On account of its cost advantages, India is nowadays the third destination[37] for R&D, just behind China and USA (WIR, 2005). It also benefits from the fact that the kind of R&D that is suited for expansion in developing countries is not very different from that which may be kept at home (WIR 2005).

Being the second most populous country in the world, India is also attractive for market-seeking FDI. Half of the population is under 25 years of age. India's consumer market is growing quickly (with an average over 12 percent a year)[38]. Living standards are rising, a vibrant middle class - estimated to 300 million- with spending power is emerging in the cities, and infrastructures needs are tremendous.

3 - Specificities of Indian investment abroad

Negligible until the beginning of the 1990s, FDI outflows from developing countries have grown faster over the past 15 years than those from developed countries (WIR 2004). The emerging of Indian MNCs, following those of China and of Asian NPI, has to be placed in such a trend.

3-1 A favourable context

In many ways, India is outstanding among outward investors from developing countries: a few Indian firms invested abroad at the beginning of the twentieth century; they mainly went in developing countries. Mafatlal (textile) invested as early as 1920 in Uganda in a cotton-spinning. Birla invested in Africa in the 1950's and in South Asia east between 1965 and 1981. Kirloskar created its first JV in Africa and South East Asia in 1971, and Ranbaxy set up its first JV abroad in Nigeria in 1977, and so on.

But Indian FDI took a new course in 2001-2002 when it became more diversified, involving a larger number of companies and countries. Buyouts performed by them would have been unthinkable several years ago. The government encouraged outward FDI and overseas M&As[39]. Even public enterprises were at the forefront of these investments. Since 2000, Oil and Natural Gas Corporation (ONGC) has set up large businesses abroad (notably in Russia on in Angola) and Indian Oil Corporation (IOC) invested massively in Libya in 2004-2005.

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[36] Indian software companies such as TCS, Wipro and Infosys, have alliances with Ericsson, Nokia and IBM

[37] For instance, in the pharmacy industry, it has been estimated that the cost of clinical development was 45% of the corresponding work in a developed country (*Goldman Sachs 2005, WIR 2005.* India is a very efficient and short way to test drugs for consumers because clinical trials are time-consuming, expensive and ethically difficult.

[38] Personal computer penetration is 9 per 1,000 persons. The cellular mobile market is expected to surge to over 70 million subscribers by fiscal year ending 2005 from the present 67 million users. The country has 54 million cable TV customers.

[39]For instance, in January 2004, the Indian government removed the ceiling of $100 million on foreign investment by Indian companies and raised it to equal their net worth.

Many Indian firms have ownership-specific advantages which spur on their investments abroad. Furthermore, Indian enterprises have comfortable financial means and can afford to invest abroad. This investment is funded by former profits, banking loans and stock markets.

India has a great number of experienced and competitive companies with capabilities in a large area of activities, from raw materials to the most cutting edges of services. They are not satisfied with exporting or being passive partners of foreign firms, they aspire to become global players.

3-2 Indian firms go first in developing countries but the share of industrial countries is increasing

Most of Indian FDI is going to other developing countries and Russia. Between 1996 and 2004, these countries received about 70% of it. Such a trend can be easily explained by the numerous proximities (geographical, social, economic), and by the need to secure Indian natural resources (industrial, energetic, agricultural), many of them being located in Africa, in Latin America and in Russia. The share of Asia has been increasing these last years: Hong Kong, Singapore, and Vietnam, taken together, accounted for 9% of total Indian FDI. This share is probably growing again in the coming years while China is becoming one of India's largest trading partners[40]. As for industrial countries, its share has been booming since 2000. North American and European countries respectively accounted for about 16 and 11 percent of Indian FDI abroad between 1996 and 2005. Indian firms are increasingly attracted by the US and EU.

[40] The top IT Indian services players have already invested in China.

Table 10 - Country-wise approved Indian Direct Investments in Joint Ventures and wholly owned subsidiaries, main countries

($ million)

	Ap1996-March 2002	2002-03	2003-04	2004-05	2005-06 (Aug 05)	**Total**
Russia	1748.68	0.15	1.43	1076.17	1.068	**2827.450**
USA	1540.83	185.27	207.14	251.73	135.83	**2320.780**
Mauritius	618.34	133.35	175.59	149.38	55.9	**1132.56**
Virgin Isl.	776.53	3.27	4.92	131.41	14.71	**930.84**
Bermuda	232.63	28.95	142.46	221.26	2.6	**627.9**
Sudan	--	750	162.03	51.55	43.13	**1006.71**
U.Kingdom	410.62	34.53	138.48	71.85	120.09	**775.58**
Hong Kong	445.12	14.8	16.15	73.64	22.22	**571.93**
Singapore	152.96	46.79	15.85	239.03	19.49	**474.12**
Australia	6.99	94.97	92.87	158.76	28.97	**382.56**
Netherlands	157.92	15.92	30.18	30.65	124.56	**359.23**
UAE	110.24	12.6	32.07	41.85	61.30	**258.06**
Vietnam	228.79	0.06	0.04	0.06	0	**228.95**
Oman	204.88	0.35	1.51	5	1.7	**213.44**
China	38.8	30	27	15	44	**153**

Source: Reserve Bank of India

Ten countries account for 86.1% of approved Indian FDI abroad since 1996.

Russia accounted for 19.9 per cent of total cumulative Indian FDI outflows due to oil and gas industries[41].

The United States is the second destination of Indian FDI: it received 16.3% of it between 1996 and 2005. It is one of the most favourite destinations of Indian FDI.

Two tax havens, Bermuda and British Virgin Islands, account together for 11 % of cumulative Indian FDI, followed by Mauritius (8%)[42]. Such privileged ranks are in relation with the important Indian Diaspora living in Mauritius and also with some round tripping investments and financial transfers[43]; however, some "true" commercial and manufacturing investments do

[41] With, notably, the acquisition of Sakhalin Oil field by the Oil and Natural Gas Commission (ONGC)

[42] The double taxation avoidance treaty between India and Mauritius have encouraged Indian firms to practice "round trip" investment through Mauritius and other tax haven countries to take advantage of the tax benefits enjoyed by overseas investors (WIR, 2005).

[43] We previously noticed that Mauritius was the main "foreign" investor in India

exist[44].

With 6.5% of Indian FDI outflows, Sudan also appears as a favourite destination. This rank is related to many investments in the oil sector. However, its share is not regular according to the years.

The United Kingdom is the sixth destination of Indian FDI (5.5% of outflows). It is a privileged destination, in relation to former colonial and human networks, and on account of the use of English by Indian businessmen.

All in all, Indian FDI in Russia, Sudan and other developing countries is mainly boosted by the research of raw materials and energy, while FDI in the United States, the United Kingdom and other industrial countries is either driven by market targets or by access to know-how and technology. As to FDI in Bermuda, Virgin Islands and Mauritius, they are mainly stimulated by financial goals.

3-3 Manufacturing industries and non financial services are prominent

Manufacturing and non financial services account for the bulk of Indian investment abroad. Between 1999 and 2005 (as of August), manufacturing industries globally represented 59% of outward FDI, and non financial services 30%. In 2004 and 2005, the share of manufacturing was very high (72.2% and 68.8% respectively). In 2005, the trading sector held the second rank (12.2%), and non-financial services the third one (12.1%).

Table 11 - Industry distribution of approved Indian outward FDI, fiscal years 1999-2005
($ million and %)

Fiscal Year	Manufacturing	Financial Services	Non-financial Services	Trading	Others	Total
1999-00	535.8	4.3	1130.7	58.3	2.3	1731.5
2000-01	370.7	16.6	876.5	89.2	29.1	1382.2
2001-02	2210.9	48.6	565.5	139.2	62.3	3027.0
2002-03	1056.7	1.8	280.2	69.9	63.7	1472.2
2003-04	756.6	35.1	438.8	76.9	134.1	1450.5
2004-05	2026.4	9.2	548.2	69.1	151.33	2804.3
2005-06(Ap-Aug05)	627.4	16.0	110.9	111.0	47.0	912.5

Source: Reserve Bank of India

Pharmaceuticals, software and IT-related services have been the main drivers of Indian FDI abroad. As early as 1975-1990, Indian FDI outflows in services went to Singapore, Thailand, Sri Lanka and Malaysia. By the 1990s, most of Indian FDI in services concentrated in developed countries, mainly in the United Kingdom and the United States (UNCTAD, 2005). However, some investors moved into selected developing-countries, especially China, South-East Europe

[44] For instance, these last years Indian firms set up in Mauritius new spinning mills, a disaster recovery centre (Infosys), and so on.

and in the CIS[45]. Indian call centres and business-process outsourcing companies started to set up foreign affiliates in countries such as the Philippines and Mexico (WIR, 2005). By 2004, the top 15 Indian software and related service companies had all invested abroad, and many TNCs (software, pharmaceutical) had global R&D operations: they focused on serving their customers in specific areas and on the acquisition of know-how.

3-4 The M&As road

In recent years, cross-border M&As have become a new mode of overseas market entry for Indian companies in many activities, and, for some of them, a key part of their growth strategy: today, while they benefit of an optimistic climate, some Indian firms go aggressively after M&As in industrial countries.

According to a recent study by Grant Thornton (2006), between 2001 and 2005 (until August), Indian companies were involved in 4690 overseas M&As in the world. These deals have been prominent in the IT software services and pharmaceutical industries, and many of them have been made in Europe (50% of deal value in 2005), and in North America (24% of deal value in 2005). The United States and the United Kingdom have been the countries that garnered the more important outbound deal share. If the number of Indian purchases has fluctuated according to the years and to the opportunities, the trend is largely increasing.

Table 12 - Cross-border Mergers & Acquisitions – Indian purchases
($ million)

Year	1998	1999	2000	2001	2002	2003	2004
Amounts of purchases	11	126	910	2,195	270	1,362	863

Source: WIR 2004, and 2005

In 2005, according to Neha Kaushik (2005), overseas Indian acquisitions could have topped 4.5 billion dollars, compared to about 2 billion in 2004. They were often made by small and medium size companies and their average amount was about 30-40 million dollars. By acquiring a partnership with a foreign firm abroad, Indian firms try to circumvent their difficulties. Setting up a subsidiary, attempting to grow organically and establishing one's brand in a new country, is quite difficult for an Indian firm, notably in industrial countries where markets are mature. M&As promote an accelerated acquisition of production facilities and capabilities, and access to strategic assets (know-how, technology, market niches, international brand names, R&D). M&As are a good way to gain a ready access to new markets (with a good approach to local consumers) and to new sales networks. M&As facilitate growth, obtaining additional products, more revenue, more labour force, more economies of scale. For instance, the ability to add employees and to broaden their range of products and services helps Indian firms to get new customers and to acquire, as quickly as possible, a critical mass and greater credibility.

[45] Commonwealth of Independent States

Table 13 - Some of the biggest Acquisitions by Indian companies in 2004 and 2005

Indian purchaser	Company purchased - Place of FDI
ONGC	Sakhalin, Russia; Royal Dutch Shell, Angola; a Refinery in Sudan; an oil filed in Brazil, …
Indian Oil Corp.	a large oil block in the Sirte Basin of Libya
Tata Steel	Nat Steel (Singapore), Millenium Steel Company - Cementhai Holding (Thailand) ($130 million)
Tata Chemicals'	Brunner Mond Group Ltd, United Kingdom ($110 million)
Reliance	Flag Telecom (USA) ; Trevira (Germany)
Ranbaxy	RPG Aventis (France)
Infosys	Expert Formation (Australia
Wipro	Nerve Wire, USA
VSNL	Tyco Global Network (USA)
Videocon	Thomson - division picture-tube, France ($289-million)
Apeejay Surrendra	Premier Foods (tea), United Kingdom (138 million)
Matrix Laboratories	Docpharma NV Belgium (for $263 million), Mchem in China, 43 % stake in Swiss firm Explora
Videsh Sanchar Nigam	Teleglobe International Holdings Ltd USA
Dr Reddy's	Betapharm, Germany
United Phosphorous	Advanta, Netherlands
Sun Pharma	Able Labs, USA
Continental Engine	Vege Motors, Netherlands
Sundram Fasteners SFL)	Peiner Umformtechnik, Textron Deutschland Germany
Bharat Forge's (BFL)	FAW Corporation (forging industry, automotive), China Carl Dan Peddinghaus Gmbh, Germany
Mittal Steel	ISCOR, South Africa

Interestingly, the big ticket deals are not only driven by the technology sector but also by traditional sectors such as pharmaceuticals, telecommunications, auto components and other manufacturing activities. Indeed, when an Indian firm buys out a foreign company, success is not quite guaranteed. A relatively easy entry on a foreign market does not mean it will be smooth sailing for the acquirers.

First, Indian companies are relative newcomers to the game of cross-border acquisitions: many of them are on a learning curve and, so, can be mistaken. It is possible they feel destabilised by the economic and social environment of the host country (cultural and legal differences). Second, the Indian firms using the M&A route to conquer new markets are not certain to be successful because they generally purchase companies which are unprofitable (it is usually the reason why they are for sale). Generally, the success or failure of M&A deals depends on the acquisition cost and on the way the integration is made.

However, most Indian purchasers are optimistic insofar as their acquisition entails synergies between, on the one hand, new local distribution networks abroad which boost their sales and, on the other hand, low-cost manufacturing based in India and the possibility to achieve higher scales of production. Some Indian firms notice that many Western companies have their own financial problems increased by stringent labour and environmental regulations prevailing in their country: this is very true in Europe where "the costs of compliance add significantly to overall manufacturing costs" (Darel , 2006).

It is sometimes considered that it is easier to set up a greenfield facility in the United States, while the M&A road is preferred in Europe (WIR, 2005). In the coming years, Europe is likely to remain a hunting ground for Indian companies seeking to acquire firms, particularly since its economy is growing slowly, "sellers are numerous and the valuations are low" (Neha Kaushik (2005).

Conclusion

Opening and FDI have really created new opportunities for India's development and boosted the performances of local firms as well as the globalization of some of them. Such a trend has undeniably raised Indian's stature among developing countries.

However, the potential of the country to catch up the levels of the leading economies in the coming decades, often touched on, is not quite guaranteed. India has an extremely hard job to perpetuate its advantages, to achieve further productivity gains and to ensure that all segments of its population participate in the income growth. The challenge that India has to take up is, in many regards, close to that of China. What is sure it is that, because of their size, of their capabilities and of their ambitions both of these emerging countries have the possibility to alter the international economic landscape over the coming generation.

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