Chapter 8

Conclusion and Policy Recommendations

The primary objective of this study was to examine the trends and patterns of Indian Outward foreign direct investments (OFDI) in terms of the magnitude, sectoral composition and direction of the flows for the last five decades. In this study an attempt was also made to empirical test the important locational determinants (pull factors) of host countries in influencing the spatial distribution of Indian overseas investments with special reference to pharmaceutical acquisitions. The study clearly attributes the changes in the OFDI pattern to the profound changes in Indian OFDI regulation. In the pre-liberalisation period, the government of India viewed Indian overseas investments sceptically as a drain of human and domestic resources, resulting in very low OFDI. However, Indian attitude to OFDI changed during the 1990s and was identified as a means to enhance the global competitiveness of the Indian industry.

8.1 Findings of the Research

The pre-liberalisation period witnessed OFDI flows being dominated by a few manufacturing sectors and largely confined to developing countries. From 1991 onwards, the scale of overseas investments was not only much larger, but was also found originating from all sectors of the economy and increasingly from the service sector. This period also witnessed a change in the direction of the flows, which was now more towards the developed countries and tended to be majority-owned projects. The motives for investing abroad also underwent significant changes to include not only market seeking types, but also to seek strategic assets. The mode of entry of most of the overseas investments has been through mergers and acquisitions and green field investments.

The current study identified the pharmaceutical industry to be the most prominent outward investor in the Indian manufacturing sector and proceeded
to conduct an empirical analysis of the most important locational determinants in the host countries that have contributed in attracting Indian pharmaceutical deals. The findings of the research address the research questions framed in chapter 5 which are reported below.

1. More than possessing some unique ownership advantages, the Indian pharmaceutical firms have been able to leverage country-specific advantages such as constant supply of qualified skilled professionals, a stable economy and government support, along with improved infrastructure to their advantage and have gained strength as one of the largest producer of low cost, high quality generic drugs. India’s country specific advantage is efficiency based rather than monopoly based which has steadily made India an attractive hub for outsourcing pharmaceutical activities to include contract research, contract manufacturing and other support activities. Strategic government policies have also significantly contributed in building the domestic production base and the development of indigenous skills which have all contributed to the successful transformation of the Indian pharmaceutical industry into a global player. Therefore, it may be suggested that Indian pharmaceutical firms have been prompted to invest in more advanced countries to access or augment, rather than to exploit their ownership advantages. But as researchers (Dunning et al., 2006) have pointed out that seeking “asset-augmenting FDI” requires significant managerial, organisational, and institutional capabilities to effectively internalise the acquired assets. It may be inferred that Indian pharmaceutical firms possess these capabilities to undertake asset seeking FDI on such a large scale.

2. The study revealed that locational factors have increasingly driven the spatial distribution of Indian pharmaceutical acquisitions. The study revealed that most of the Indian pharmaceutical companies were increasingly acquiring firms in technologically advanced countries to augment their product development capabilities. The empirical results also revealed that the economic environment of the host country in terms of the corporate taxation regimes and inflation levels also influenced the choice of
destination. While institutional variables such as rule of law and political stability of the host country appeared to be prerequisites for the Indian acquiring firms, the presence of corruption in host countries did not impact Indian foreign acquisitions. This indifference to the presence of corruption could be due to the familiarity for the Indian firms of working in similarly weak institutional environments. The openness of the host countries in terms of pursuing liberal policy regimes also turned out to be an important and positive determinant of direction of acquisitions.

3. The main motives behind the internationalisation strategies of Indian pharmaceutical firms have been for acquiring new product portfolios, brands, research laboratories and technologies for overcoming their technological deficiencies and to strengthen their innovative capabilities. Such strategic asset seeking FDI has been instrumental in bringing new tangible and intangible assets to the Indian pharmaceutical firms. Another important motivation behind the internationalisation has been to develop a presence in key strategic countries such as USA, U.K, Germany and other developed countries to establish their legitimacy in technologically advanced industries such as pharmaceuticals. With Indian pharmaceutical companies (IPCs) still lacking superior product development capabilities, they have been increasingly using the inorganic route of acquisitions in overseas markets as a strategy.

4. The current study shows that due to absence of vast resources, inadequate technological capabilities and marketing networks, the Indian pharmaceutical firms have followed the linkage, learning and leverage model to quicken their pace of internationalisation. They have established several kinds of linkages by entering into cross border activities via inter firm relations and also by starting their own subsidiaries and affiliates in different strategic overseas markets. Apart from undertaking green-field investments, they are also aggressively acquiring overseas business enterprises, brands and research facilities and are thereby, constantly learning from such linkages and leverages.
5. Regarding the kind of linkages sought by Indian pharmaceutical firms in their cross-border investments, the study found that in the first stage of multinational growth, the linkages were in the form of joint ventures, while in the second stage the linkages were through mergers and acquisitions which helped the Indian pharmaceutical companies in the assimilation of new skills and technology. Indian firms are leveraging their existing capabilities in process R&D by entering generic markets in advanced countries such as the US and Europe.

6. The study also reveals that physical distance between the home and host countries was not a deterrent for acquiring foreign firms. Therefore contrary to the predictions of the Uppsala model, Indian pharmaceutical firms have not internationalised only into foreign markets that are close to the domestic market in terms of psychic distance but also in countries which are far away from the home country. The study identifies the presence of a common language such as English between India and the host countries as an important factor in reducing the psychic distance as it appears that English speaking countries seem to be preferred choice of destination as the presence of a common language facilitates better communication and reduces transaction costs.

8.2 Contribution of the Research

Since OFDI from India is a relatively recent phenomenon, studies in this area have been few. The insights from this research suggest that rapid changes in the world economy brought about by globalisation, has led to the establishment of new approaches and patterns of internationalisation of firms from emerging markets. The strategic innovations and the new modes of internationalisation adopted by the developing country MNEs have not been captured by existing theories. The current research contributes to the scant literature by focussing on the internationalisation of firms from developing countries.
Secondly, the research establishes strongly the critical role played by liberalisation and market-friendly national policies undertaken at appropriate times to not only initiate domestic capability building from an almost non-existent production base but also for the successful transformation of the Indian pharmaceutical industry into a globally competitive player. If the timely policy interventions had not taken place, Indian pharmaceutical industry might have continued to be dependent upon imports of bulk drugs and foreign firms might have continued to simply distribute imported drugs and charging maximum prices. The empirical testing of the locational choice model as in the case of the Indian pharmaceutical industry contributes to the small empirical literature in this field.

8.3 Suggestions for Policy

In the recent years, Indian overseas investments have increasingly been seen not only as a means to integrate itself with the global economy but also as an optimal strategy to development, growth and self reliance. Set against this backdrop, there is a need to put in place a set of policy guidelines and framework which could create a conducive environment for Indian enterprises to increasingly undertake overseas direct investment. Essentially, these policy guidelines should aim at incentivising Indian firms to undertake overseas direct investments

1. Streamlining administrative procedures through decentralization of authority to local governments
2. Easing capital controls
3. Providing information and guidance on investment opportunities
4. Establishing processes for reducing political and other non-commercial investment risks; and
5. Expanding bilateral investment agreements for investment protection.
While some of these measures have already been initiated, it is suggested that a specific institutional mechanism be in place and act as the nodal agency for all policy guidance and issues related to outbound investments from India on an exclusive and proactive basis.

The current study observed that the RBI data on overseas direct investments only captures the actual flow of funds rather than the ultimate destination of fund flows. The RBI data on joint ventures and wholly owned subsidiaries (JV/WOS) captures only the immediate recipients of the Indian investments, which very often, are merely intermediaries that do not have any operations or may be routed through layers of shell companies or SPVs, to take advantage of the tax treaties between different countries, making it difficult to identify the actual destination of investments. This may result in distorting the extent of integration between India and the rest of the world in terms of actual outward investments. In this context, it is suggested that RBI should monitor the end-use of cross-border investments and make it mandatory for firms to report not only the first but also the final destination of their overseas investments. It is suggested that the Indian government may seek inspiration from China’s ‘Going Global’ policy for its firms to promote Indian overseas activities. Initiating measures such as developing a series of guidance documents that provides information about prospective host countries in terms of their investment climates, trade related laws and regulations, taxation policies and industry opportunities for Indian companies will help in the reduction of not only research costs but also investment risks for Indian companies.

The success story of the Indian pharmaceutical industry can be an important learning model for other developing countries that are keen to internationalise rapidly. The main learning experience is that in developing countries, government intervention is indispensible to initiate the process of capacity building. Other developing countries, following Indian experience, can increase their public investments in pharmaceutical research, research institutions and laboratory facilities, and in skill creation like training of pharmaceutical scientists, engineers, as essential policy tools. Given its
commitment to the policy of south-south cooperation, India should continue to transfer technologies to fellow developing countries and benefit from operating synergies.

Indian policy-makers may encourage overseas acquisitions, as they not only enhance competitive advantages by providing access to new product portfolios, technology and skills, but also ensure an established marketing and distribution networks. The policy makers may, therefore, take suitable measures to remove barriers for Indian companies to acquire overseas business. Besides allowing the overseas acquisition applications to go through the automatic route, the Indian government could also lay out an appropriate support programme such as provision of cheap credit for acquisition and insurance coverage against political risks. Given the high cost and risks involved in acquiring overseas businesses, the Indian firms should have access to consultancy services in evaluating the acquisition opportunities in overseas market. The policy makers may also invest in the development of human resource and management training to successfully integrate the foreign firm with the domestic entity, given the cross cultural differences and varied business practices and legal system. The Indian government may also provide low-cost finance for research along with subsidy facilities to promote indigenous research activities.

8.4 Limitations of the Study

The locational choice model in the current study has been confined only to the Indian pharmaceutical industry. In the empirical model, the deal value of pharmaceutical acquisitions could not be considered as a dependent variable, as most of the times the deal value is not disclosed by companies. Also due to unavailability of data of some of the independent variables, some acquisition deals could not be considered for analysis. Another important limitation of the study is that the study focuses on only the country specific advantages in attracting FDI while firm-specific advantages are not within the scope of the study.
8.5 Future Scope of the Study

In the empirical model, the deal value of pharmaceutical acquisitions could not be considered as a dependent variable, as a large proportion of Indian acquisition deals were not disclosed. The study may be extended by considering the deal value to study the locational preferences of Indian acquiring firms. Further, the study can combine firm specific advantages along with country specific advantages to understand the spatial spread of Indian FDI. The same empirical model may also be extended to other sectors of the Indian economy to examine the diversity in the motivations of Indian FDI. A comparative analysis of FDI flows between India and other emerging markets may also be undertaken to get a better picture of the paradigm shifts taking place in international production.

8.6 Managerial and Theoretical Implications

The current research shows that a multinational firm’s FDI location decision is determined by a host of multi-level factors suggesting the following managerial and theoretical implications. The firm owners and managers need to be aggressive in their efforts to discover untapped international opportunities to remain competitive and to enhance their firm specific technological capabilities. The study reveals that the preferred mode of entry for the Indian companies has been the acquisition strategy, which involves various market and operational risks. Identifying the right target markets and companies is the challenge and possessing sufficient knowledge about the host country environment is a must otherwise the stakeholders face the risk of delays and increasing transaction costs. Host country governments desirous of attracting Indian FDI, on their part should also strive to liberalise their policy regimes and facilitate a conducive economic, institutional and political environment.
The theoretical implications of our findings suggest that the existing theories on the internationalisation strategies of emerging market multinationals do need an overhaul since the choice of investment location of the Indian firms does not conform to the mainstream theories. They have deviated from the conventional path of choosing neighboring and other emerging economies to target developed economies in pursuit of their strategic intent. Future researchers can develop new theories, which can adequately explain the internationalisation strategies of emerging market multinationals.