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TREND ANALYSIS AND POLICY FRAMEWORK FOR OFDI IN INDIA- A CONCEPTUAL STUDY

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Abstract

The concept of globalization with its momentum has replaced the terms 'domestic' or 'global', to Glocal – Global plus Local. Indian companies have adopted the 'Overseas Direct Investment' route to gain latest technology, assets, skills, resources and new markets. This research paper highlighted the trend and patterns adopted by Indian companies by Foreign Direct Investment Outflows. This research analysed the data 10 years from April 2007 to April 2017, collated it annually, and then cumulated together for making inferences. The policy framework of Foreign Direct Investment Outflows in India revealed the government's intentions to nurture and support the development of Indian companies' investments abroad by creation of Foreign Investment Facilitation Portal and the Bilateral Investment Promotion and Protection Agreements. The overall trend of the overseas investments was positive. The equity participation in the overseas investments was 28%, the loans 16% whereas the Guarantee Issued by the Indian companies was 56%. Lastly, analyzing the mode of investments revealed that 24% of the investments made during the last decade were Joint Ventures and 76% of the investments made were WOS.

Keywords:

Foreign Direct Investment Outflows;

OFDI;

OFDI Trends;

Policy Framework.

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1. Introduction

The concept of Global businesses or globalization is now gaining such a momentum worldwide that instead of the terms 'domestic' or 'global' used in contrast with each other, the businesses are now commonly being considered Glocal – Global plus Local. The wave of privatization and globalization has reached and penetrated at such a level in the world that making your business go global isn't a dream but a necessity if you have to survive the changes and competitive environment cropping up all around.

Making your business competitive and growing continuously involves a lot of changes and adaptation according to the changing business strategies. One of them is getting investment from a foreign entity in the form of Foreign Direct Investment. FDI inflow is considered to be an important and key factor for development. But it is not only the inflow that decides the growth of the company, but also the overseas direct investment that the company is making, that are generally termed as Outward Foreign Direct Investment (OFDI). For the global growth of the business, exports were the first and major instrument that the business firms chose. But since past two decades the growth of Foreign Direct Investment Outflow shows that exports are not the only key mechanisms that firms chose today to globalise their operations (Refer figure 1).

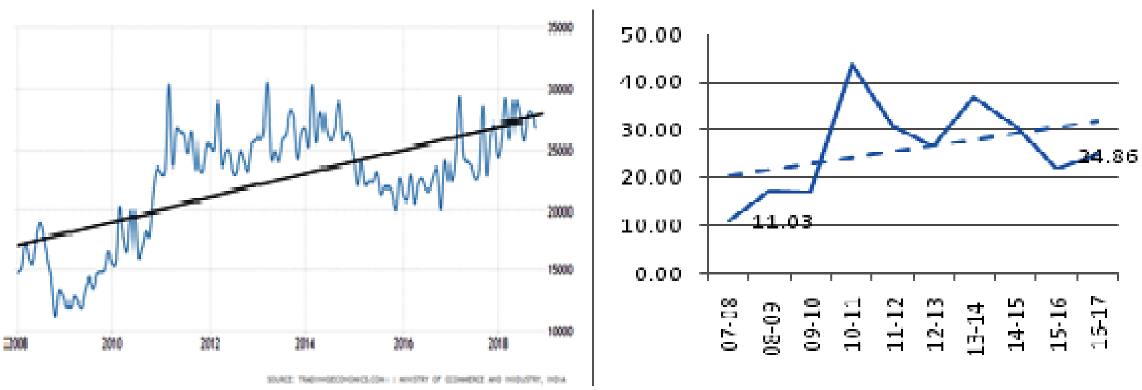

Figure 1: Exports and OFDI for 10 years (2008-2018)

Source: Compiled from RBI data and tradingeconomics.com

According to the recent UNCTAD World Investment Report 2018, the global foreign direct investment (FDI) flows fell by 23 per cent in 2017 compared to 2016. FDI that accounted for $1.87 trillion in 2016 fell to $1.43 trillion in 2017. But the other macroeconomic indicators like GDP and trade, showed a better picture of growth. The report also highlights that FDI flows fell in developed and transition economies, whereas developing economies remained more or less stable comparatively, and accounted $671 billion for 47 per cent share of the global inflows in 2017 compared to 36 per cent in 2016. India stood at the 11th position among the top 20 FDI recipient economies.

The Department of Economic Affairs, in their factsheet on Overseas Direct Investment (ODI) updated that the cumulative amount of actual ODI outflows from India from April 2014 to December 2017 amount to US$ 39546.58 million. The amounts of ODI outflows for the past 3 years has been published in the factsheet as US$ 6800.86 million for 2014-15, US$ 10620.19 million for 2015-16, US$ 14801.21 for 2016-17 and US$ 7324.33 for 2017-18 (data collected till December 2017). The factsheet also highlights that the sectors involved in maximum ODI are the Manufacturing sector and the Financial, Insurance and Business Services sector with cumulative outflows amounting to US$ 11787.26 million and US$ 11458.19 million respectively. Similarly the top three destinations for ODI investment are seen to be Mauritius, Singapore and United States of America with a cumulative ODI outflow of US$ 8036.22 million, US$ 7884.45 million and US$ 5655.31 million respectively.

With the facts throughout it can be clearly observed that Indian companies are seeking advantages by adopting the Overseas Direct Investment route in order to gain access to latest technology, assets, skills, resources and new markets. Earlier patterns of investment in ODI reveal that India invested majorly in developed countries to gain advantages of FDI outflow but its recent investments in countries like Mauritius, Singapore, the Netherlands and British Virgin Islands reveal that Indian companies are also looking into the provisions of tax benefits that these countries offer as a decision criteria for investment.

Looking into various researches done in the past, the major factors for India's OFDI decisions may be assumed to be expansion, entering new markets, acquisition of new technical know-how, regulatory changes, saturation in Indian markets, natural resources availability in the host country, need to develop the export competitiveness and other firm specific objectives.

This research paper tries to highlight the concept of Overseas Direct Investment or Foreign Direct Investment Outflows (OFDI) from India and the trend and patterns adopted by companies in the country towards this investment option. This research has analysed the data from the

Reserve Bank of India (RBI) website from the Overseas Investment Division for a time span of 10 years from April 2007 to April 2017. The monthly data available has been collated annually and then cumulated into total OFDI made by the country. The paper presents a trend analysis for the OFDI based on the last decade and tries to conclude on the direction of the trend. In the later section of the paper, the sectoral patterns and the mode of investments (whether Joint Ventures or Wholly Owned subsidiaries) adopted in the direct investments abroad are also analysed.

2. Literature Review

The Outflow of Foreign Direct Investment from India is been observed and seen to be consistent right from the pre-liberalization period. In the keynote address by Mrs. Shyamala Gopinath (as the Deputy Governor of Reserve Bank of India) at the International Conference on Indian cross-border presence/acquisitions in 2007, she highlighted that the evolution of overseas direct investment is seen in two distinct phases, the pre-2003 phase and the post-2003 phase.the prior being export oriented with restrictions on cash flows and the later being the phase where liberalization of the automatic route allowed Indian firms to invest abroad in large scale. The development is not only marked by the changes in the policy framework in the OFDI but also the geographical spread and sectoral composition of the investments done by Indian companies in the overseas market. The major literature regarding the overseas direct investment or OFDI in India is been presented in this section.

- Export-import bank of India’s research paper, (May 2014) titled “Outward direct investment from India: Trends, Objectives and Policy Perspectives”. The paper has highlighted that the scenario for OFDI in India is changing at a faster rate. Based on their primary research, the major drivers of OFDI include regulatory changes in the country, expansion, low factor cost advantages, technical know-how. The paper expresses a need for a set of policy guidelines and framework with the establishment of Overseas Investment Promotion Council.
- Divya Chaudhry, Priyanka Tomar and Pallavi Joshi (March 2018) in their paper titled “Deconstructing Indian Overseas Foreign Direct Investments” have put forth the discussion about the trends that OFDI had followed in India in two waves of internationalization, the pre and post liberalization phase of the economy. It is also observed that favourable investment climate is crucial for Indian companies OFDI. It is suggested that Indian enterprises try to

broaden their presence in markets of developed economies through mergers and acquisitions while greenfield investments are adopted as mode of entry in developing countries.

- Ravi Subramanian, Charu Sachdeva & Sebastian (2010) highlighted that post liberalization, specifically since the last decade it is seen that the FDI outflows from India have gained momentum. The paper suggests that the earlier part of their investment abroad, many companies are seen to adopt the forming alliances or joint ventures while enteruing foreign markets, and at a later stage, move towards Greenfield investments after their experience.
- Supriya Chopra and Satvinder Kaur Sachdev (2014) enumerated in their research that FDI encourages the incorporation of new inputs and technologies in the production systems of host countries. It is also concluded that FDI outflow has multilayered structures and the motivations for investment range from genuine business/commercial considerations to taxation benefits which are available to any global investors. The System, procedures and basic infrastructure can be developed to attract more FDI and also things to be taken care of in case of fast track clearance systems and system for legal disputes.
- Ms. Parul Mittal and Mr. Sandeep Aggarwal (2012) enumerating on the FDI Inflows and Outflows in India stated that international trade and FDI in an economy are seen as important catalysts for economic growth, especially the developing economies. And also emphasize that India needs massive investment to achieve the goal of 20-20.
- Dr. O.S. Doel (2017) in his paper the last decade has seen a lot of change in the pattern and composition of global outward foreign direct investments. It was also pointed out that Indian companies' OFDI patterns show that they prefer investing in those economies where the chances for economic growth are high and the government is seen to be effective in managing and controlling practices such as corruption and malpractices.
- India Brand Equity Foundation in their article "Indian Investment Abroad - Overseas Direct Investment By Indian Companies‟ (2018) have Indian investment abroad earlier were focused towards nations with good resources such as Australia, UAE, and Sudan. But it was later observed that this pattern is changing and Indian MNCs (Multi National Corporations) are investing in countries such as Mauritius, Singapore, and the Netherlands that provide good tax benefits.
- Vrushali Pakhannavar and Dr. Basavaraj Kudachimath (2018) in their research paper have highlighted that the RBI has liberalized guidelines for Indian companies' foreign

investments abroad by raising the annual overseas investment ceiling to US$ 125,000 from US$ 75,000 to establish JV (Joint Venture) and WOS (Wholly Owned Subsidiaries). The government's supportive policy regime complemented by Indian firms' experimental outlook could lead to an upward trend in OFDI in future.

3. Research Methodology

This paper has undertaken research from available secondary data sourced through government department websites like Reserve Bank of India (RBI), Department of Department of Industrial Policy & Promotion (DIPP), Department of Economic Affairs (DEA), etc. for analysis and interpretations. The worldwide data is sourced mainly through international organizations like Organisation for Economic Co-operation and Development (OECD) and United Nations Conference on Trade and Development (UNCTAD).

The researcher has compiled the monthly data for Overseas Direct Investment (ODI) from 2007 to 2017 published by RBI on its website. The study has adopted the 'Time-series, Trend Analysis' method for making conclusions on the discussions made.

Objectives of the Study

- To study the conceptual framework of OFDI
- To analyse the policy framework of OFDI in India
- The analyse the trends of OFDI from India, and mode of investment adopted by firms.
- To study the country-wise pattern adopted by Indian companies to make investment abroad.

4. Conceptual Framework of Outward Foreign Direct Investment

According to the RBI guidelines provided (along with FEAM regulations) "Direct investment outside India" means investment by way of contribution to the capital or subscription to the Memorandum of Association of a foreign entity or by way of purchase of existing shares of a foreign entity either by market purchase or private placement or through stock exchange, but does not include portfolio investment.

RBI prohibits Indian Parties from making investment (or financial commitment) in foreign entity engaged in real estate (meaning buying and selling of real estate or trading in Transferable Development Rights (TDRs) but does not include development of townships, construction of residential/commercial premises, roads or bridges) or banking business, without the prior approval of the Reserve Bank. Also, an overseas entity, having direct or indirect equity participation by an Indian Party, shall not offer financial products linked to Indian Rupee.

Direct Investment outside India is allowed under the Automatic route or the approval route. The Indian Party has been permitted to make investment / undertake financial commitment in overseas Joint Ventures (JV) / Wholly Owned Subsidiaries (WOS), as per the ceiling prescribed by the Reserve Bank from time to time. The eligible limit under the automatic route is 400% of the net worth as per the last audited balance sheet. Currently any financial commitment exceeding USD 1 billion in a financial year is the ceiling limit w.e.f. July 03, 2014. The Investment (or financial commitment) can be made through Special Purpose Vehicle (SPV) under Automatic Route or an Issue of guarantee by an Indian Party to step down subsidiary of JV / WOS.

Investment (or financial commitment) in unincorporated/ incorporated entities overseas in oil sector under the Automatic Route (i.e. for exploration and drilling for oil and natural gas, etc.) by Navaratna PSUs, ONGC Videsh Ltd (OVL) and Oil India Ltd (OIL) is permitted by AD Category - I banks, without any limit, provided such investments are approved by the competent authority (Refer Figure 2).

According to the OECD, “Foreign Direct Investment (FDI) is a category of investment that reflects the objective of establishing a lasting interest by a resident enterprise in one economy (direct investor) in an enterprise (direct investment enterprise) that is resident in an economy other than that of the direct investor. The lasting interest implies the existence of a long-term relationship between the direct investor and the direct investment enterprise and a significant degree of influence (not necessarily control) on the management of the enterprise. The direct or indirect ownership of 10% or more of the voting power of an enterprise resident in one economy by an investor resident in another economy is the statistical evidence of such a relationship.”

Broadly speaking, FDI is composed of three distinct modes of financing, namely, equity capital (which refers to purchase of an enterprise's share by a foreign investor in a foreign country), reinvested earnings/profits in the host country (share of earnings of a foreign direct investor which is neither given out as dividends by foreign affiliates nor remitted to the home country), and intra-company debt transactions (short or long-term borrowing and lending of finances between foreign direct investor and affiliate enterprises) (Divya Chaudhry, Priyanka Tomar & Pallavi Joshi, March 2018).

In India, the Department of Economic Affairs (DEA) provides that data relating to the monthly and annual FDI outflows along with the approvals as well. But does not provide for the sectoral composition or the country-wise detailed analysis for the same. Whereas the Reserve Bank of India (RBI) provides the monthly OFDI statistics for the investment from India. But even this data to some extent is based on the financial commitments of the corporate rather than the actual investments done. And part of this data available on the government sources is provisional and subject to change on account of online reporting made by the dealer banks of the companies. This proves that the OFDI in its true nature is a dynamic process and hence keeping a track of this data in real-time is a very challenging task.

Another most important point to be noted while discussing the nature of OFDI is that the data that is available points towards the first investment made by the parent company in the overseas market, but it does not capture the further redirected investments that these companies in the host countries make at a later stage.

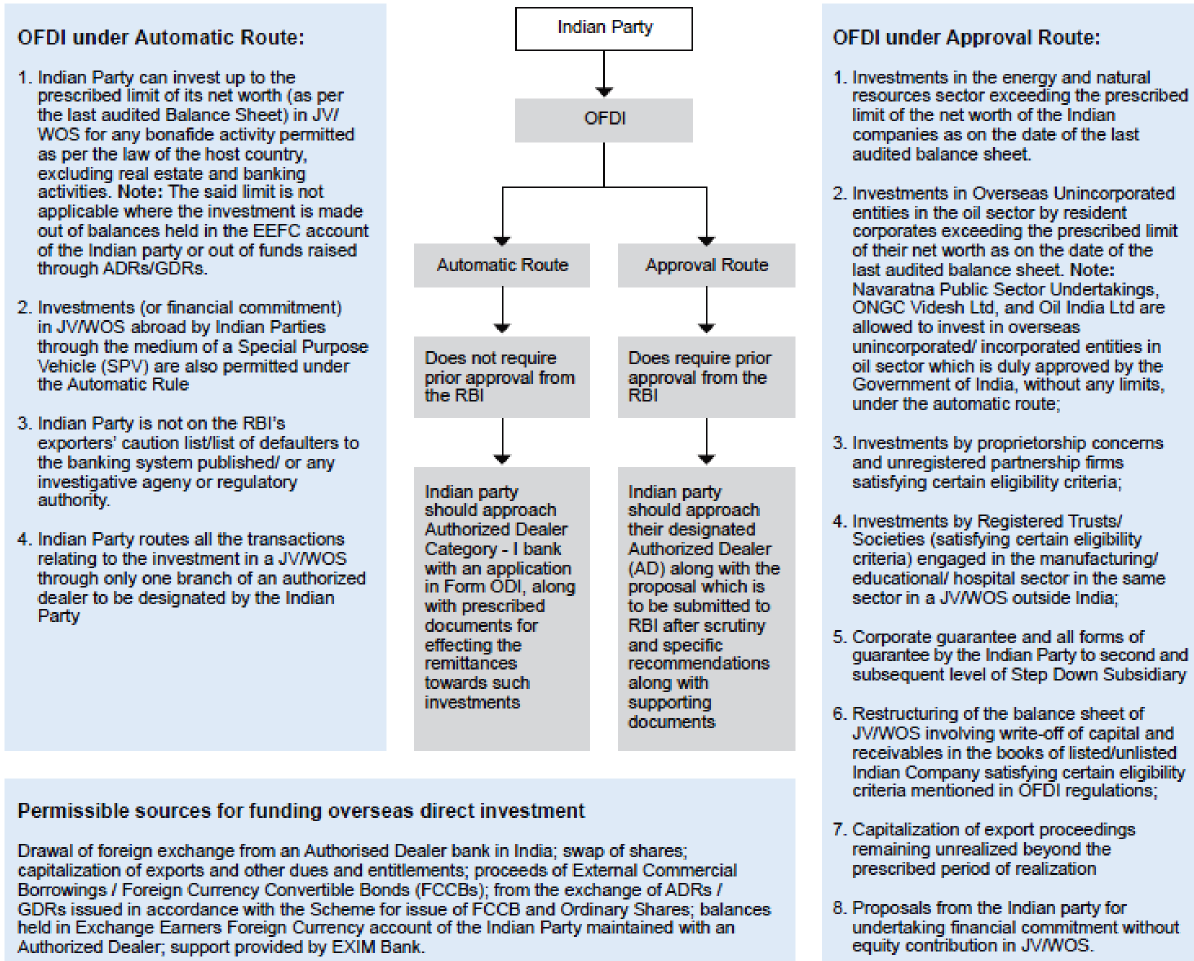

Figure 2: Framework of OFDI in India

Source: Divya Chaudhry, Priyanka Tomar and Pallavi Joshi (March 2018)

5. Policy Framework for OFDI

To continue the wave of OFDI after liberalization, the Reserve Bank has been progressively relaxing the rules and simplifying the procedures both for current account as well as capital account transactions in the country. The creation of Foreign Investment Facilitation Portal and the Bilateral Investment Promotion and Protection Agreements (BIPAs) are also a step towards developing India's footprint in the overseas markets.

The Foreign Investment Facilitation Portal (FIFP) is the new online single point interface of the Government of India for investors to facilitate Foreign Direct Investment in India. This portal is being administered by the Department of Industrial Policy & Promotion (DIPP), Ministry of

Commerce & Industry. Subsequent to abolition of the Foreign Investment Promotion Board (FIPB) by the Government in 2017, the work of granting government approval for foreign investment under the extant FDI Policy and FEMA Regulations, has been entrusted to the concerned Administrative Ministries/Departments.

The eleven notified sectors/activities requiring government approval are Mining, Defence/cases relating to FDI in small arms, Broadcasting, Print media, Civil Aviation, Satellites, Telecom, Private Security Agencies, Trading (Single, Multi brand and Food Products), Financial services, not regulated or regulated by more than one regulator/ Banking Public and Private (as per FDI Policy) and Pharmaceuticals.

The Department of Industrial Policy and Promotion (DIPP), Ministry of Commerce & Industry has been given the responsibility of overseeing the applications filed on the Foreign Investment Facilitation Portal and to forward the same to the concerned Administrative Ministry. A Standard Operating Procedure (SOP) developed by DIPP in consultation with the concerned Administrative Ministries is being followed for processing of the FDI applications. Approval letters in Standard Format will be uploaded on the Portal itself for the benefit of the Investors. The Guidelines for Investors is the Consolidated FDI Policy circular and Press Notes as updated from time to time.

6. Indian OFDI: Trends And Patterns

The overseas investments in India began in the early 1960s with large business houses like Tata, Birla and Kirloskar, who sought for enhancing their production activities through entering the foreign markets by investing in cross-border activities in countries like Africa and Sri Lanka. But the concept of OFDI can be credited to the introduction of the 1991 economic reforms in the country. This can be seen with the OFDI estimates provided by UNCTAD where India’s OFDI flows were seen to be US$ 44 million during 1980-89 and soared to US$ 79.3 billion during 2000-09. The trend and evolution of OFDI in India is divided into two parts i.e. The first wave (1975-90) and the Second wave (1991 onwards) and the actual volume of OFDI from India can be assessed only after the year 1999-2000 since data for OFDI and portfolio investments were not disaggregated until then. (Priyanka Tomar and Pallavi Joshi, 2018).

This paper has compiled the RBI data for a span of 10 years from 2007 to 2017 for studying the trend of OFDI in India. Table 1 provides the data relating to the last decade of OFDI investments made by Indian companies in the overseas market. It is observed that the amount of OFDI has increased from USD 11029.84 million in 2007-08 to USD 24863.05 million in 2016-17 which is more than doubled in the period.

Year	*Financial Commitment*			*Total*
	Equity	*Loan*	*Guarantee Issued*	
2007-08	6074.68	2387.17	2568.00	11029.84
2008-09	10713.55	3329.00	3100.83	17143.38
2009-10	6345.94	3193.13	7215.33	16754.40
2010-11	9351.77	7346.89	27230.52	43929.18
2011-12	6288.35	8325.17	16249.38	30862.91
2012-13	5856.20	4350.96	16665.22	26872.38
2013-14	10194.50	3725.51	22980.48	36900.49
2014-15	3985.73	2852.94	24080.85	30919.52
2015-16	4753.76	3354.45	13908.42	22016.63
2016-17	9301.93	4106.78	11454.34	24863.05
Total	*72866.40*	*42972.01*	*145453.37*	*261291.77*

Table 1: Outward FDI from India (Amount in USD million for 2007-17)

Source: Data Compiled from RBI statistics

Though the growth of foreign direct investment outflows from India had a positive trend since the 2000, it was observed that during the span of 2006 to 2010 there was a slow movement of funds from the country in the terms of the OFDI values. This can be attributed to the global meltdown faced by many economies during that time span which affected all major economies dependent on the United States of America, but Indian economy was not comparatively affected. But Indian firms were seen to avoid OFDI during that time period in particular. The overall trend of the Foreign Direct Investment Outflows however illustrates a positive growth (as shown in Figure 3).

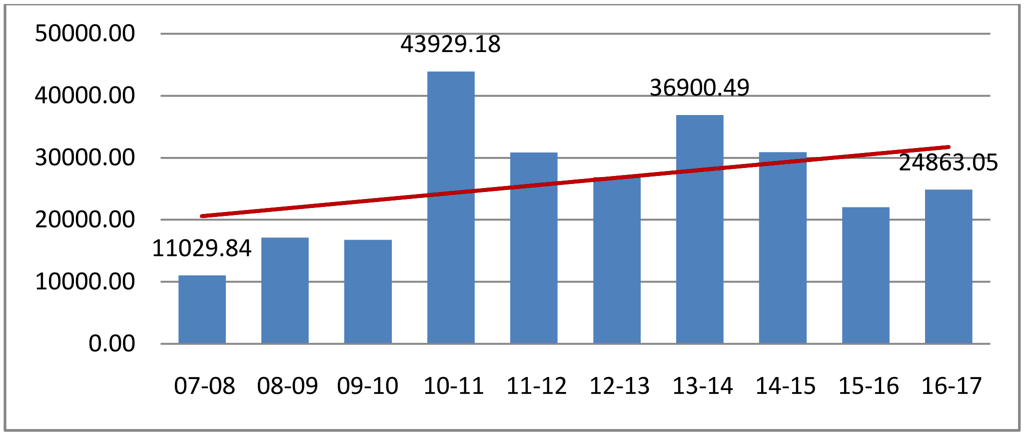

Figure 3: The trend of OFDI in India for the past decade

Source: Data Compiled from RBI statistics

The major changes observed in the trend of the OFDI investments reveal that the years 2007-08, 2010-11, 2013-14 and 2016-17 were the ones that tried reviving the otherwise declining trend of the OFDI investments in the countries with USD 11029.84 million, USD 43929.18 million, USD 36900.49 million and USD 24863.05 million respectively.

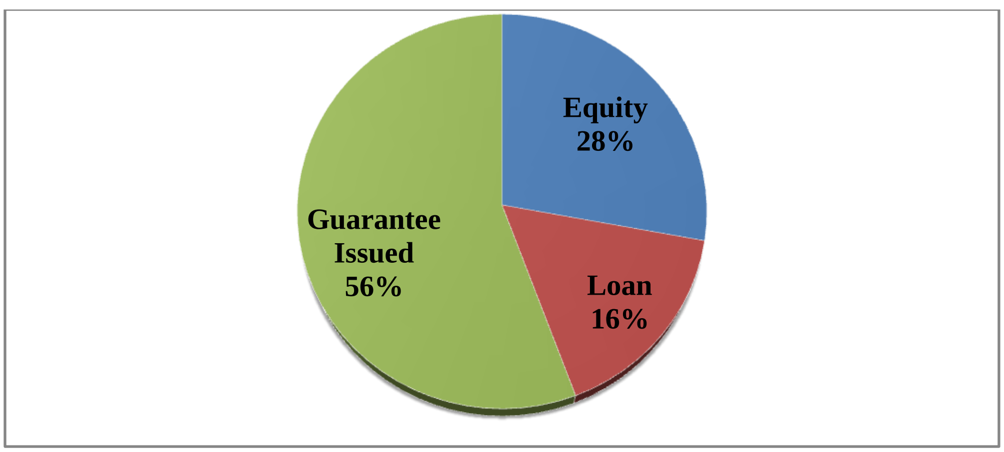

Figure 4: The Financial Commitment in OFDI in India for the past decade

Source: Data Compiled from RBI statistics

As far as understanding the financial commitments is concerned, the OFDI figures for the time period demonstrate that equity participation in the foreign firms was adopted as the strategy by 28% of the investments made during the span. The facts also portray Debt or loans to be the most minimum opted for strategy with only a 16% of contribution towards the investments being made. Whereas the guarantee issued by the firms towards its existing Joint Ventures (JVs) and Wholly Owned Subsidiaries (WOS) illustrate to be the most preferred strategy for expanding their overseas markets as this figure tends to be the maximum among the strategies adopted at level of 56% of the total investments considered (Refer Figure 4).

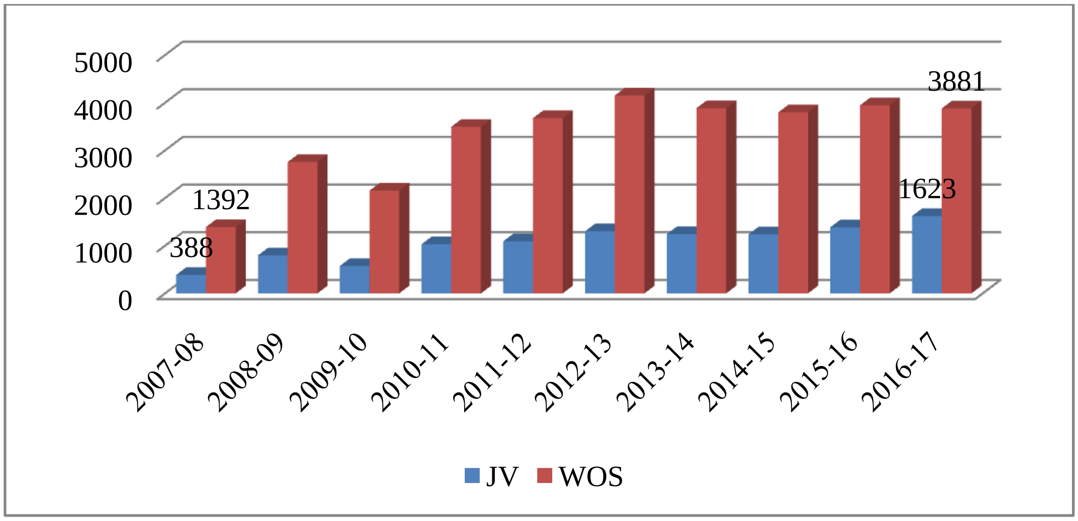

Figure 5: Mode of Investment (JV/WOS)

Source: Data Compiled from RBI statistics

When the modes of investments are discussed, choosing whether the overseas investment will be made by a JV or a WOS is to be decided. The past data that were analysed proved that both Joint Ventures and Wholly Owned Subsidiaries are being adopted by Indian Companies to mark their foot in the overseas market. Data analysis reveals that out of a total of 43806 deals recorded, 10674 were Joint Ventures and 33132 were Wholly Owned Subsidiaries, that is to say 24% of the investments made during the last decade were JV and 76% of the investments made were WOS (Refer Figure 5).

7. CONCLUSION

For the global growth of the businesses in India, exports were the first and major instrument that the business firms chose. But since past two decades the growth of Foreign Direct Investment Outflow shows that exports are not the only key mechanisms that firms chose today to globalise their operations. Indian companies are seeking advantages by adopting the Overseas Direct Investment route in order to gain access to latest technology, assets, skills, resources and new markets, and companies are now seen to be investing in developing economies along with developed economies as well to gain advantages such as expansion and tax benefits. The policy framework of the OFDI in India clearly reveals the country's intentions to nurture and support the development of Indian companies' investments abroad. The policy changes and updating done in the FEMA rules, the creation of Foreign Investment Facilitation Portal and the Bilateral Investment Promotion and Protection Agreements, portrays a positive support towards the overseas direct investments in the economy. The pattern and trends of OFDI are clearly visible though the investments which show that the amount of OFDI has increased from USD 11029.84 million in 2007-08 to USD 24863.05 million in 2016-17, which is more than doubled in the period. The overall trend for OFDI for the time span considered seems to be positive. The equity participation in the financial commitments is seen to be 28%, the loans are 16% whereas the Guarantee Issued by the Indian companies during this span in highest at 56% of the total investments. Lastly analyzing the mode of investments revealed that 24% of the investments made during the last decade were Joint Ventures and 76% of the investments made were WOS. OFDI in its true nature is a dynamic process and hence keeping a track of this data in real-time is a very challenging task. Most of India's publicly available data on OFDI should be interpreted carefully.

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