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Outward Foreign Direct Investment from India

Trends, Issues and Destination Determinants

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Abstract: *Outward foreign direct investment from India has grown fast since 2005-06 owing to inward and outward FDI policy liberalisation in India. This Paper analyses the trends in outward foreign direct investment from India. It also discusses the up-coming issues in context of India's outward foreign direct investment. At the same time, it analyses empirically the determinants of geographical destination of India's outward foreign direct investment. The outward foreign direct investment flows from India rose from US$ 678 million in 2000-01 to US$ 13989 million in 2013-14. Till 2005-06, outward FDI from India has mainly been by way of equities and loans. From 2006-07, funding of overseas FDI by issue of guarantee has also become an important way for Indian companies. The sectoral pattern of outward FDI shows that it has been mainly invested in services and manufacturing sector. The recent trend is showing that outward FDI form India is increasingly flowing to developed countries. Outward FDI from India to developed countries have been mainly through mergers and acquisitions, while the mode of entry to developing economies has mainly been through green-field investments. The real GDP growth in host countries and an efficient governance system in host countries seem the main driver of outward foreign direct investment from India. . It seems that inflation rate in host economy is not considered at all while deciding the location of outward foreign direct investment from India.*
Keywords: *Outward FDI, Host countries, India, Real GDP growth, Government effectiveness*

I. Introduction

Foreign direct investment is natural extension of process of globalisation that usually begins with exports. In the process, enterprises try to access markets or resources or technologies available overseas. Eventually, enterprises gradually try to reduce the cost of production and transaction by expanding overseas production operations in countries where certain ownership-specific advantages can help them to compete globally. The emergence of Indian transnational corporations on the international scene was a phenomenon of early 1960s when a few big Indian business conglomerates such as the Tata, the Birla and the Kirloskar began to expand their production activities trans-border by investing in Africa and Sri Lanka. The growth of phenomenon of Indian enterprises investing abroad has been more rapid after 1991 economic reforms. The rise in the propensity of Indian enterprises to undertake international production is being driven by several internal and external factors. The important internal factors include the process of industrialisation along with the accumulation of skills and technological capabilities and liberalisation of trade and liberal inward and outward FDI policies. The overseas foreign direct investment provide the domestic enterprises better access to global networks and markets, transfer of technology and skills and enables them to share research and development efforts and outcomes. In the Indian context, overseas investments have been primarily driven by either resource seeking or market-seeking or technology-seeking motives. Of late, there has been a surge in resource seeking overseas investments by Indian enterprises, especially to acquire energy resources in Australia, Indonesia and Africa (H R Khan, 2012).

The study has the following objectives:

1. To examine the current trends of outward foreign direct investment flows from India with a view to understand the geographical destination, sectoral composition and mode of financing.
2. To discuss the potential issues in context of outward FDI from India.
3. To ascertain the macroeconomic factors in the host country determining the flow of outward FDI from India.

To attain the primary objective of the study the following hypotheses have been made:

1. Null Hypothesis (H_0): Macroeconomic fundamentals in the host economy are the main determinants of outward foreign direct investment from India.
2. Alternative Hypothesis (H_1): Outward foreign direct Investment from India is not influenced by the macroeconomic fundamentals in the host economy.

The following section discusses the trends in the flow of global outward foreign direct investment during 2001 to 2014. Section 3 mentions about the main policy changes in India in context of overseas foreign direct investment since 2003. Section 4 shows the trends in terms of sectoral composition, funding composition and destinational composition of outward foreign direct investment from India during 2000-01 to 2013-14. The

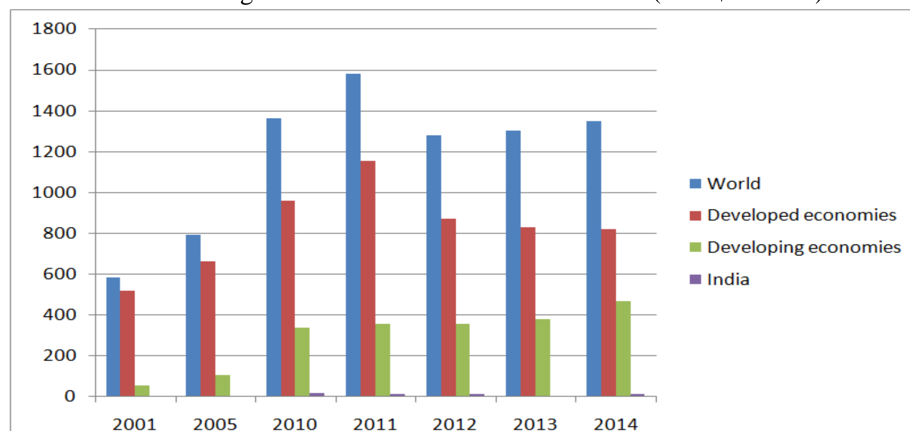
emerging issues regarding outward foreign direct investment from India have been discussed in Section 5. Section 6 presents the empirical results of this study in context of destination determinants of outward foreign direct investment from India. Section 7 concludes the study.

II. Global Outward Foreign Direct Investment

The changes in policy environment across the economies have altered the composition and pattern of global outward foreign direct investment flows and stocks as well. Diagram 1 shows the pattern of global foreign direct investment flows. The global outward foreign direct investment flows, which were equal to US$ 584 billion in 2001, rose to US$ 1354 billion in 2014. The outward flows of foreign direct investment from developing countries rose from US$ 58 billion in 2001 to US$ 468 billion in 2014, while their share in global outward foreign direct investment flows increased from 10% to 35% during this period. The outward foreign direct investment flows from India, which were US$ 1.4 billion in 2001, rose to US$ 10 billion in 2014. The trend shows the growing importance of developing countries in global outward foreign direct investment flows. This is happening due to policy changes and globalisation of the economies across the globe, in which emerging economies are playing the leading role.

Diagram 1

Global Foreign Direct Investment- Outward Flows (U.S. $ billions)

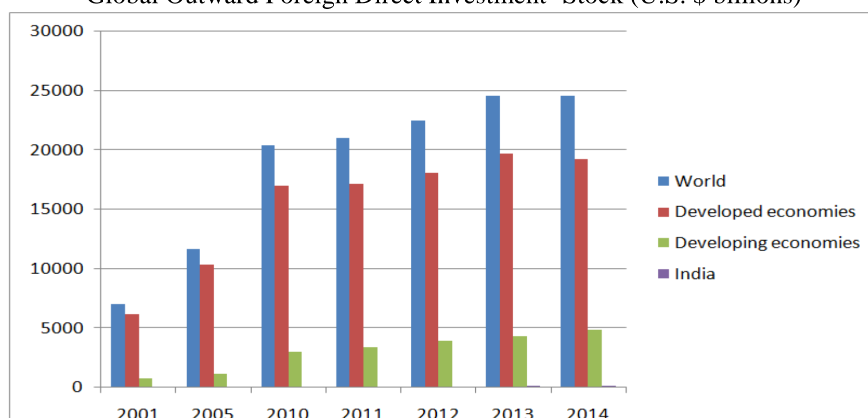


Source: UNCTAD Stat

Diagram 2 shows the composition of global stock of outward foreign direct investment. The global stock of foreign direct investment increased from US$ 7006 billion in 2001 to US$ 24602 billion in 2014. The stock of outward foreign direct investment from developing countries increased from US$ 753 billion in 2001 to US$ 4833 billion in 2014, resulting in increase of their share in global stock of foreign direct investment from 11% in 2001 to 20% in 2014. The stock of outward foreign direct investment from India increased from US$ 3 billion in 2001 to US$ 130 billion in 2014. The share of developing countries in global stock of outward foreign direct investment has gradually increased over the years to 20%. This shows the economic integration of developing countries in the world economy. This happening due to relaxations in capital controls in developing economies resultant to policy changes.

Diagram 2

Global Outward Foreign Direct Investment- Stock (U.S. $ billions)



Source: UNCTAD Stat

III. Overseas Investment Policy Liberalisation

Guidelines for overseas investment by Indian firms were existed before the process of liberalisation and globalisation of Indian economy in 1991-92. Guidelines were quite restrictive and subject to the condition of no cash remittance and mandatory repatriation of dividend from the profits from overseas projects. Overseas investments in joint ventures and wholly owned subsidiaries have been recognised as important channels for promoting global business by Indian entrepreneurs. Changes in overseas investment policy were started in 1991keeping in view the changing needs of the growing economy. With a stable rise in the capital inflows, particularly in the second half of 2000s, the overall foreign exchange reserve position provided comfort to progressive relaxation of the capital controls and simplification of the procedures for outbound investments from India. The three phases of overseas investment guidelines liberalisation mentioned below can be explicitly counted in the development of the outward FDI policy of India.

Phase I (1992-95): The period of Economic Liberalisation in India

The 'automatic route' for overseas investments by Indian entrepreneurs was introduces in 1992. The cash remittances were allowed for the first time. However, the total value was restricted to US$ 2 million with a cash component not exceeding US$ 0.5 million in block of 3 years.

Phase II (1995-2000): Conception of Fast Track Route

A comprehensive policy framework was laid down in 1995 and the work relating to approvals for overseas investment was transferred from Ministry of Commerce to the Reserve Bank of India to provide a single window clearance mechanism. In overseas investment policy framework, a fast track route was initiated where the limits were raised from US$ 2million to US$ 4 million and linked to average export earnings of the preceding three years. The cash remittances continued to be restricted to US$ 0.5 million. Above US$ 4million, approvals were considered under the normal route approved by a Special Committee comprising senior representatives of the Reserve Bank of India (Chairman) and the Ministries of Finance, External Affairs and Commerce (members). Investment proposals in excess of US$ 15 million were considered by the Ministry of Finance with recommendations of the Special Committee and were generally approved if the required resources were raised through the global depository receipts (GDR) route.

The exchange earners, other than exporters, were brought under the fast track route in 1997. Indian promoters were authorized to set up second and subsequent generation companies subject to the first generation company was set up under the fast track route. The condition that the amount of outward investment should be repatriated in full by way of dividend, royalty, etc within a period of five years was done away. A series of measures to encourage software industry in India to expand capacity, reduce costs, improve quality and invest abroad introduced.

Phase III (2000 onwards): Liberalisation under FEMA and Thereafter

Though the process of economic liberalisation in India began in 1991, the scope of outward FDI expanded significantly after the introduction of the Foreign Exchange Management Act (FEMA) in June 2000. The substantial liberalisation of overseas investment policy took place since 2003 owing to improvement in the macroeconomic fundamentals of the economy. The build -up in the foreign exchange reserves had supported the process of liberalisation of a number of capital controls including the overseas foreign direct investment from India. The liberalisation measures were initiated by both- the Reserve Bank of India and the Government of India. Table 1 exhibits policy initiatives taken in regard to overseas investment since 2003.

The automatic route for overseas direct investment was further liberalised in March 2003 to enable Indian parties to invest to the extent of 100% of their net worth. Since then the limit of overseas FDI has been gradually increased to 400%. The ceiling of 400% of net worth, however, is not applicable for

(i) Investment made out of balances held in the Exchange Earners' Foreign Currency (EEFC) account of the Indian Party or out of funds raised abroad through ADRs/GDRs.
(ii) Indian companies engaged in the energy and natural resources, such as, oil, gas, coal and mineral ores, though they would require prior approval of the Reserve Bank of India.

Access to international financial markets was also progressively liberalised for the Indian corporate sector and they were allowed to use special purpose vehicles (SPVs) in international capital markets to finance their cross border acquisitions. The Reserve Bank of India progressively enhanced the limits for overseas investments by mutual funds, eligible firms, trusts and unregistered partnership firms. The automation through a web-based application has enabled efficient processing of applications which has reduced the processing time and at the same time made the management information system more efficient. The RBI also automated the entire process of allocation of Unique Identification Number (UIN).

Fifty percent of the amount of performance guarantee issued by the Indian party was allowed to be reckoned for the purpose of computing financial commitment to its joint ventures/wholly owned subsidiaries abroad. Indian parties were allowed to extend corporate guarantee on the behalf of the first generation step down operating company under the Automatic Route subject to the limits.
Since July 2011, the Reserve Bank of India is disseminating the data on outward FDI from India on a monthly basis.

The Government of India has drafted tactical plans to promote overseas investment by Indian firms. The Government of India approved a policy to support purchases of raw material assets made by public sector undertakings abroad. In April 2010, Indian companies were allowed to participate in a consortium with other international operators to construct and maintain submarine cable systems on a co-ownership basis under the automatic route. Public sector undertakings in agriculture, mining, manufacturing and electricity sectors having a three year record of making net profits are eligible are exempted from the government approval for investing up to US$ 50bn abroad. The Ministry of External Affairs and Indian missions abroad would be associated in a buyout process from the launch.

Table 1

Major changes in Overseas Investment Policy

Period	Relaxation in policy
March 2003	The automatic route of overseas investment up to US$ 100mn allowed to Indian corporate with a proven track record for investment in overseas joint ventures or wholly owned subsidiaries, even where the investment is not in the same core activity as they are engaged. They were also allowed to invest in such ventures up to 100% of their net worth.
January 2004	Investment in overseas joint venture/ wholly owned subsidiaries up to 100% of their net worth was allowed for eligible Indian entities without any separate monetary ceiling.
May 2005	Allowed to invest up to 200% of their net worth. The ceiling is not applicable to investment made out of balance held in EEFC accounts and proceeds of ADRs/GDRs.
March 2006	Under the Automatic Route, Indian parties allowed to disinvest without prior approval of RBI subject to certain conditions. The proprietary/partnership unregistered firms with a proven track record and a consistently high export performance were allowed to set-up joint venture/wholly owned subsidiaries outside India with prior approval of RBI.
July 2006	Aggregate ceiling for overseas investments by MFs increased from US$ 1bn to US$ 2bn.
April 2007	VCFs permitted to invest in equity and equity related instruments of off-shore venture capital undertakings subject to overall limit of US$ 500mn.
June 2007	The limit under the Automatic Route enhanced from 200% to 300% of net worth.
September 2007	The limit under the Automatic Route enhanced from 300% to 400% of net worth. The aggregate ceiling for overseas investment by mutual funds was enhanced from US$ 4bn to US$ 5bn. The limit of portfolio investments enhanced from 35% to 50% of net worth of investing company as on the date of last audited balance sheet.
April 2008	The aggregate ceiling for overseas investment by mutual funds was enhanced from US$ 5bn to US$ 7bn.
June 2008	Indian companies were allowed to invest in excess of 400% of their net worth as on the date of last audited balance sheet in the energy and natural resources sectors abroad.
August 2008	Registered Trusts and Societies engaged in manufacturing/educational sectors allowed to invest in the same sector in joint ventures/wholly owned subsidiaries overseas with the prior approval of RBI.
May 2011	Indian promoters of WOS abroad or having at least 51 percent stake in joint venture abroad allowed to write off capital or other receivables in respect of the joint ventures/wholly owned subsidiaries.
June 2011	Indian parties were allowed to disinvest without prior approval of the RBI, where the amount repatriated on disinvestment is less than the amount of the original investment with certain conditions.

Source: RBI Press Releases

IV. Trends In Indian Outward Foreign Direct Investment

Indian firms started to invest overseas in 1960s, albeit India's restrictive policies for overseas investment limited them to small, minority joint ventures in developing economies. Sustained growth in Indian overseas investment could be seen starting during 1970s when the industrial licensing system was more rigid. India has emerged as an important overseas investor due to (i) rapid economic growth, (ii) easy access to financial resources and (iii) strong motivations to acquire resources and strategic assets abroad. The trend analysis shows that the level of outward FDI from India has grown manifold since 2000-01. Table 2 shows that outward foreign direct investment flows rose from US$ 678 million in 2000-01 to US$ 13989 million in 2013-14. The flows of outward FDI witnessed a sharp increase during the second half of 2000s as compared to the first half. The global financial crisis affected the flow of outward FDI from India in 2009-10. Though, a sharp rebound in outward FDI flow was seen in 2010-11.

Till 2005-06, outward FDI from India has mainly been by way of equities and loans. From 2006-07, funding of overseas FDI by issue of guarantee has also become an important way for Indian companies. The share of financing outward FDI through equities declined from 88.8% in 2000-01 to 73.4% in 2013-14, while share of loans in financing outward FDI from India rose from 10.5% to 26.4% during the corresponding period.

The financing of outward FDI from India through issue of guarantee, which was mere US$ 113 million in 2000-01 rose substantially to US$ 22980 million in 2013-14.

Table 2

Actual Outflows in Respect of outward FDI (U.S $ millions)

Period	Equity	loan	Guarantee invoked	Total	Guarantee issued
2000-01	602 (88.8)	71 (10.5)	5 (0.7)	678 (100)	113
2001-02	879 (87.9)	121 (12.1)	0 (0.0)	1000 (100)	156
2002-03	1746 (94.4)	102 (5.6)	0 (0.0)	1848 (100)	140
2003-04	1250 (79.8)	317 (20.2)	0 (0.0)	1567 (100)	441
2004-05	1482 (74.3)	513 (25.7)	0 (0.0)	1995 (100)	315
2005-06	6658 (84.8)	1195 (15.2)	3 (0.0)	7856 (100)	547
2006-07	12063 (90.6)	1247 (9.4)	0 (0.0)	13310 (100)	2261
2007-08	15432 (83.4)	3075 (16.6)	0 (0.0)	18507 (100)	6553
2008-09	12477 (67.2)	6102 (32.8)	0 (0.0)	18579 (100)	3322
2009-10	9393 (68.4)	4297 (31.6)	24 (0.2)	13714 (100)	7603
2010-11	9235 (54.8)	7556 (45.2)	52 (0.3)	16843 (100)	27059
2011-12	4577 (44.8)	5637 (55.2)	0 (0.0)	10214 (100)	16411
2012-13	5853 (57.4)	4349 (42.6)	0 (0.0)	10202 (100)	16664
2013-14	10264 (73.4)	3725 (26.6)	0 (0.0)	13989 (100)	22980

Note: 1. Figures in parenthesis represent percentage.
Source: RBI and www.careratings.com

Table 3 shows the sectoral composition of outward FDI flows from India during 2008-09 to 2013-14. The sectoral pattern of outward FDI shows that it has been mainly invested in services and manufacturing sector. Within manufacturing, major sub-sectors which attracted outward FDI from India included agriculture machines and equipments, basic organic chemicals, drugs, medicines and allied products, refined petroleum products, indigenous sugar etc. Similiarly, within services sector, a majority of outward FDI had gone into business services, data processing, financial services, architectural and engineering, and other technical consultancy services.

Table 3

Indian Outward Foreign Direct Investment- Sectoral Distribution
(Amount in U.S. $ billions)

Sector	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14*
Transport, storage & communication services	0.31 (1.7)	0.38 (2.8)	0.82 (4.8)	1.82 (17.7)	1.46 (14.3)	1.25 (12.2)
Manufacturing	10.18 (54.7)	5.35 (39.1)	5.04 (29.9)	2.87 (28.1)	3.60 (35.3)	2.47 (24.2)
Agriculture & mining	2.38 (12.8)	0.95 (6.9)	1.21(7.2)	0.44 (4.3)	0.33 (3.2)	3.63 (35.5)
Wholesale, retail trade, restaurants, & hotels	1.17 (6.3)	1.13 (8.2)	1.89 (11.2)	1.14 (11.2)	0.70 (6.9)	0.62 (6.1)
Financial, insurance, retail & business services	3.55 (19.1)	4.41 (32.2)	6.53 (38.8)	3.16 (30.9)	2.84 (27.8)	1.26 (12.3)
Construction	0.35 (1.9)	0.36 (2.6)	0.38 (2.3)	0.37 (3.6)	0.63 (6.2)	0.15 (1.5)
Community, social & personal services	0.39 (2.1)	0.18 (1.3)	0.70 (4.2)	0.18 (1.9)	0.48 (4.7)	0.82 (8.0)
Electric, gas & water	0.14 (0.8)	0.84 (6.1)	0.10 (0.6)	0.04 (0.4)	0.05 (0.5)	0.02 (0.2)
Miscellaneous	0.12 (0.6)	0.11 (0.8)	0.18 (1.0)	0.19 (1.9)	0.11 (1.1)	0.00 (0.0)
Total	**18.58 (100)**	**13.71(100)**	**16.84 (100)**	**10.21 (100)**	**10.20 (100)**	**10.22(100)**

Note: 1. (*) Figures for April 2013 to January 2014.
2. Figures in parenthesis represent percentage.
Source: RBI and www.careratings.com

Table 4 depicts destinational distribution of outward FDI from India during 2008-09 to 2013-14. The recent trend is showing that outward FDI form India is increasingly flowing to developed countries. This reflects growing confidence of the Indian corporate and availabilities of resources at competitive rates. The off-shore centres in Netherlands, Singapore and Mauritius have been major destinations for outward FDI from India. "During 1961-1989, 82% of Indian outward FDI went to other developing countries; but in 1990-2007, almost 62% went to developed countries (Pradhan and Suavant, 2010).

Outward FDI from India to developed countries have been mainly through mergers and acquisitions, while the mode of entry to developing economies has mainly been through green-field investments. The main reason for mode of mergers and acquisitions in developed economies is that markets are mature there and companies prefer to gain market share through acquisitions rather than green-field investments.

Table 4
Indian Outward Foreign Direct Investment- Geographical Destination
(Amount in U.S. $ billions)

Economy	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14*
Netherlands	2.79 (15.0)	1.53 (11.2)	1.52 (9.0)	1.24 (12.1)	0.82 (8.0)	1.17(11.4)
Singapore	4.06 (21.9)	4.20 (30.6)	3.99 (23.7)	2.14 (21.0)	1.68 (16.4)	1.05(10.3)
British Virgin Islands	0.00 (0.0)	0.75 (5.5)	0.28 (1.7)	0.53 (5.2)	0.49 (4.8)	3.21 (31.4)
Mauritius	2.08 (11.2)	2.15 (15.7)	5.08(30.2)	2.97 (29.1)	2.22 (21.8)	1.08 (10.6)
U.S.A.	1.02 (5.5)	0.87 (6.3)	1.21(7.2)	0.92 (9.0)	1.35 (13.2)	0.90(8.8)
U.A.E.	0.63 (3.4)	0.64 (4.7)	0.86 (5.1)	0.45 (4.4)	0.63 (6.2)	0.21(2.1)
U.K.	0.35 (1.9)	0.34 (2.5)	0.40 (2.4)	0.46 (4.5)	0.56 (5.5)	0.37 (3.6)
Switzerland	0.00 (0.0)	0.00 (0.0)	0.25(1.5)	0.17 (1.7)	0.52 (5.1)	0.81(7.9)
Cayman Islands	0.00 (0.0)	0.04 (0.3)	0.44 (2.6)	0.14 (1.4)	0.02 (0.2)	0.09 (0.9)
Hong Kong	0.00 (0.0)	0.00 (0.0)	0.16 (0.99)	0.33 (3.2)	0.07 (0.7)	0.03 (0.3)
Others	7.65 (41.1)	3.19 (23.2)	2.65 (15.7)	0.86 (8.4)	1.84 (18.0)	1.30(12.7)
Total	**18.58 (100)**	**13.71 (100)**	**16.84 (100)**	**10.21 (100)**	**10.20 (100)**	**10.22(100)**

Note: 1. (*) Figures for April 2013 to January 2014**.**
2. Figures in parenthesis represent percentage.
Source: RBI and www.careratings.com

In 2005, Indian companies were allowed to float special purpose vehicles (SPVs) in international capital markets to finance acquisitions abroad facilitating the use of leveraged buy-outs. Since then, SPVs setup in off-shore financial centres, such as, the Netherlands, Mauritius and Singapore, have been mainly used as conduits to mobilise funds and invest in third countries mainly keeping in view the business and legal consideration, taxation advantages and easier access to financial resources in the countries.

The funding of overseas FDI investments is allowed in a number of ways. The sources mainly include (a) purchase of foreign exchange on-shore from an authorised dealer in India, (b) capitalisation of foreign currency proceeds to be received from a foreign entity on account of exports, fees, royalties for supply of technical knowhow or other expertise, (c) swapping of shares of Indian entity with those of foreign entity, (d) use of balances held in Exchange Earners' Foreign Currency (EEFC) accounts of Indian entity maintained with an authorised dealer, (e) foreign currency proceeds through ECBs and FCCBs, and (f) Exchange of ADRs/GDRs issued in accordance with the scheme for issue of Foreign Currency Convertible Bonds. Though, banks in India are usually not authorized to fund the equity contributions of promoters, financial assistance to Indian companies by the domestic banks for acquisition of equity in overseas joint ventures/wholly owned subsidiaries or in other overseas companies, new or existing, as strategic investment has been allowed. In order to make possible such financial support to overseas Indian business, the Reserve Bank of India has improved prudential limit on credit and non-credit facilities extended by bank to Indian joint ventures and wholly owned subsidiaries abroad.

V. Emerging Issues In Outward FDI From India

Overseas direct investment from India represents relatively new aspect of India's integration into global economic and political systems. Investing overseas by India is not a target by itself, rather a means to an end. The end is development, growth and self reliance of Indian economy in the years to come. There is need of a balanced approach to be evolved by having strong policy guidelines which could help Indian enterprises to actively seek opportunities overseas, especially in the manufacturing sector and at the same time, safe guarding the domestic industry and the economy as well. The outward capital flows from India pose some issues before the economy as mentioned below:

1. One important issue that warrants close monitoring of capital outflows is the implications for domestic investment. There is need to ensure that overseas investment by Indian companies do not dampen domestic investments. There is need to examine the potential impact of rising trend in overseas FDI on domestic investment, growth and employment. It should be examined against the benefits that domestic companies gain somewhere else in terms of expanded market base, backward and forward vertical integration and economical skilled labour.

   Though in globalised economic environment it becomes inevitable to establish overseas presence of domestic enterprises, there is need of a balanced approach for domestic business expansion and compulsions of outward FDI investments.
2. Since India is a current account deficit economy, there is need to have surplus on capital account so as to finance its current account deficit. The build-up of foreign exchange reserves in last years has supported the initiatives of liberalisation of many of the capital controls including the overseas foreign direct investment from India. Unlimited capital outflows for overseas investment on part of liberalisation of capital controls

could have implications for sustainability of India's current account deficit and external debt. In this regard a cautious approach should be adopted.

3. In recent years, there has been sharp and sudden rise in the non-fund exposures in the form of issue of guarantees by Indian companies towards the joint ventures and wholly owned subsidiaries abroad. Such substantial issue of guarantees could be a potential risk for Indian banks and companies. A cautious approach is needed to mitigate impact of contingent liabilities in uncertain global economic environment.
4. There is risk involved overseas business models for a variety of reasons. There is risk of spill over of economic down-turn of foreign economies to domestic economy. Such economic down-turns may adversely impact the financials of the Indian companies with a spill-over effect on the domestic corporate and banking system.
   There is risk of appropriation of business or loss in value due to internal accruals or funding constraints that may be faced by Indian companies abroad. Indian enterprises who have acquired overseas investments at much higher premium in a bullish phase or did not take due diligence before making such investments in anticipation of future growth, may risk large valuation loss in during the economic downturn.
5. One important issue is related to abuse of multilayered structure. The motivations for overseas investment range from genuine business/commercial considerations to taxation benefits which are available to any global investor. This issue should be addressed by providing a transparent policy framework of multilayered structures for outward FDI.

Though a number of policy measures regarding overseas direct investment from India are already in operation, these need to be crystallised and brought under one umbrella. The establishment of a specific institution mechanism for promoting and monitoring overseas direct investments by Indian companies can serve the purpose well. Within the Ministry of Finance, the creation of a separate division- Indian Overseas Investment Promotion Council- can be made. Such move will help in fast tracking, monitoring, supervision and feedback mechanism of overseas direct investment from India. Another important issue is of data dissemination regarding overseas direct investment by Indian enterprises. The RBI data on overseas direct investments by only captures the actual flows of funds rather than the ultimate destination of investments. The main limitation of the RBI data on joint ventures and wholly owned subsidiaries is that it depicts only the immediate recipient nations of the investment, many of them merely intermediate without having any operations. These investments pursue intricate and obscure structures and mostly routed through multiple layers of shell companies and SPVs, primarily to leverage upon the tax treaties between different set of countries, making it difficult to identify the actual destination of investments. Therefore, data disseminated by RBI on overseas investment could lead to unclear picture of the extent of the linkage between India and the rest of world in terms of actual outward direct investments. The RBI should make it mandatory for firms to report not only the first but also final destination of their overseas investments. Here a supervisory institution, like the one proposed above, can play a role in monitoring, supervision and feedback mechanism of overseas direct investment – like some operational in other countries e.g., China.

VI. Location Determinants Of Outward Foreign Direct Investment

This section is concerned with the ascertainment of determinants of location choices of outward FDI from India. Despite the surge in India's outward foreign direct investment over the past decade, there have been very few studies on the topic and even less on the determinants of the geographical destination of India's ODI. Fung and Garcia Herrero (2012) use an augmented gravity model to examine the determinants of Indian and Chinese ODI. Their results suggest that Indian companies prefer destinations that are smaller but richer and further away. They also find that Indian investments are attracted to less corrupt economies with better rule of law while Chinese investments are attracted to more corrupt economies. They note that fuels as well as food exporting countries are preferred by Indian investment although technology acquisition and presence of ores and metal is found to be an insignificant factor in aiding investments from India. Pradhan and Sauvant (2010) note that during 1961-1989, 82% of Indian ODI went to other developing countries, but in 1990-2007, almost 62% went to developed countries. Nunnenkamp et al (2012) look into the determinants of India's ODI with the help of a gravity model and find that India's outward FDI is hardly explained by a search of resources or superior technologies. Further, they find that market-related factors appear to have dominated the location choices of Indian direct investors and that larger Indian Diaspora in the host countries attracts more ODI from India.

In a more descriptive than empirical tone, Govindarajan and Ramamurti (2010) note that India's outward FDI is led by highly entrepreneurial private firms that have capabilities in design, production, branding and distribution, and more innovative at providing products and services of "good enough" quality at ultra low prices. Rashmi Banga (2006) using data for 13 developing economies of East, South and South-East Asia argues that ODI from developing countries is basically determined by trade flows. She also finds inward FDI flows as one of the drivers of outward FDI. Ali J. Ai-Sadig (2013) using data from 121 developing and transition

economies over the period 1990-2011 shows a robust negative relationship between outward FDI from developing economies and the rate of domestic investment in these countries.

Since there are few studies and even giving diverse results regarding the destination determinants of outward FDI from India, it becomes imperative ascertain the factors in the host economy attracting outward FDI from India. To accomplish this objective, the ordinary least squares method is employed to panel data consisting 22 economies for the period spanning 2009 to 2012, in total 88 observations. The data are compiled from the Reserve Bank of India, UNCTAD and World Bank publications. The following multiple regression model has been employed to ascertain the location determinants of outward FDI from India.

$ODI = C + b_1DIS + b_2FDS + b_3RGR + b_4INF + b_5TOP + b_6GOE$

Where, C: Constant

b: Regression coefficient

ODI: Annual outward direct investment from India (US $ mn) to host economy i in year t,

DIS: Distance between host country and India in kilometres,

FDS: Foreign Direct Investment stock (in US $ mn) of host economy i in year t,

RGR: Real GDP growth of host economy i in year t,

INF: Inflation rate in host economy i in year t,

TOP: Trade openness in host economy i in year t, and

GOE: Government effectiveness in host economy i in year t.

Analysis of destination determinants of outward FDI from India is conducted in two stages. In first stage, all the main variables have been included. In the second stage, the variables not strongly associated with the outward FDI from India have been dropped. Conclusions are drawn on the basis of results of two stages. The results of regression analysis are summarised in table 5. Stage I results show that real GDP growth and the government effectiveness in host countries seem main determinants of choices of destination for outward FDI from India.

Table 5

Destination determinants of Outward FDI from India

Variable	Stage I			Stage II		
	Coefficient	t-value	p-value	Coefficient	t-value	p-value
C	-157.39	-0.453	0.65	-59.78	-0.321	0.75
DIS	-0.038	-1.082	0.28			
FDS	0.0002	1.144	0.25			
RGR	39.51	1.628	0.10	62.23	2.814	0.00
GOE	404.16	1.979	0.05	375.65	3.000	0.00
INF	58.96	1.248	0.21			
TOP	0.851	0.748	0.46			
R^2	0.19			0.13		
Adjusted R^2	0.13			0.11		
AIC	16.32			16.29		
D.W. Stat	0.67			0.57		
F-value	3.09			6.40		
Probability	0.01			0.00		

While physical distance plays a role in deriving outward foreign direct investment flows from India, it is not major one. The distance coefficient is negative and statistically insignificant. The bulk of India's outward foreign direct investment has been in the U.S. and Europe, which are significantly far away. The stock of foreign direct investment in the host countries seems positively related to outward foreign direct invest from India, albeit it not statistically significant.

The coefficient of inflation rate in the host countries is positive. This indicates that inflation rate in the host countries is not decisive factor in destination choice of outward foreign direct investment from India. The inflation rate in host country is ignored while deciding the geographical destination of outward foreign direct investment from India.

The coefficient of trade openness in host economies is positive. Countries having a high degree of trade openness are preferred destinations for India's outward foreign direct investment. But, it is not a major driver of India's outward foreign direct investment as it not statistically significant. Host country's efficacy of governance and its ability to control corruption have a positive impact on outward foreign direct investment flows from India. This result is statistically significant at 5% level of significance. Indian multinational companies seek destinations which offer a high degree of independence from political pressures, credible and pro-business government policies and a low incidence of corruption. The need for effective governance could be mainly due

to the fact that private sector companies in India major player in outward foreign direct investment from India. These private sector enterprises seek minimal government interference and greater operational freedom.
Apart from government effectiveness, real GDP growth in host country seems major driver of outward foreign direct investment from India. The regression coefficient of real GDP growth in host country is statistically significant at 10% level of significance.

In the first stage analysis, inflation rate in host economy seems ineffective in deciding the location of outward foreign direct investment from India. According analysis, FDI stock in host country, trade openness of host country and distance of host country from India seem somewhat decisive in locational choices of outward foreign direct investment from India, but not the major drivers. Real GDP growth in host economy and the government effectiveness in host economy seem major and significant destinational drivers of outward foreign direct investment from India.

In second stage, four independent variables viz., distance between host country and India, FDI stock in host economy, inflation in host economy and trade openness in host economy are dropped from regression analysis model. Two variables- namely, real GDP growth and the government effectiveness in host economy are included in the model to confirm their effectiveness in deciding the location choices of outward foreign direct investment from India. The results of stage II reflects that real GDP growth in host country and government effectiveness in host country are important factors in determining the location choices of outward foreign direct investment from India. The results are statistically significant even at 0% level of significance.

The above results and analysis indicate that India companies prefer making outward foreign direct investments in the economies where chances of economic growth are better and government is effective in controlling corruption and malpractices. The null hypothesis that Macroeconomic fundamentals in the host economy are the main determinants of outward foreign direct investment from India is accepted. These findings support the conclusion drawn by Fung and Garcia (2012) that Indian investments are attracted to less corrupt economies with better rule of law while Chinese investments are attracted to more corrupt economies. Distance between host economy and India, trade openness of host country and FDI stock in host economy also seem little bit effective in determining the location choices of outward foreign direct investment of Indian companies. It seems that inflation rate in host economy is not considered while deciding the location of outward foreign direct investment from India.

VII. Conclusions

The pattern and composition of global outward foreign direct investment has changed during last two decades. The share of developing countries in global outward foreign direct investment flows has risen to the level of 35%. There has been tremendous growth in outward foreign direct investment from India since 2005-06. There has been shift in composition, trend, funding ways and issues as well in context of outward foreign direct investment from India. The following conclusions have been drawn on the basis of this study:

1. The changes in policy environment across the economies have altered the composition and pattern of global outward foreign direct investment flows and stocks as well. The global outward foreign direct investment flows, which were equal to US$ 584 billion in 2001, rose to US$ 1354 billion in 2014. The outward flows of foreign direct investment from developing countries rose from US$ 58 billion in 2001 to US$ 468 billion in 2014, while their share in global outward foreign direct investment flows increased from 10% to 35% during this period.
   The stock of outward foreign direct investment from developing countries increased from US$ 753 billion in 2001 to US$ 4833 billion in 2014, resulting in increase of their share in global stock of foreign direct investment from 11% in 2001 to 20% in 2014.
2. The outward foreign direct investment flows from India, which were US$ 1.4 billion in 2001, rose to US$ 10 billion in 2014. The stock of outward foreign direct investment from India increased from US$ 3 billion in 2001 to US$ 130 billion in 2014.
3. Guidelines for overseas investment by Indian firms were existed before the process of liberalisation and globalisation of Indian economy in 1991-92. Guidelines were quite restrictive and subject to condition of no cash remittance and mandatory repatriation of dividend from the profits from overseas projects.
   With a steady rise in the capital inflows, particularly in the second half of 2000s, the overall foreign exchange reserve position provided comfort to progressive relaxation of the capital controls and simplification of the procedures for outbound investments from India. The Reserve Bank of India has relaxed certain limits related to outward foreign direct investment from India. The Government of India has drafted tactical plans to promote overseas investment by Indian firms.
4. Till 2005-06, outward FDI from India has mainly been by way of equities and loans. From 2006-07, funding of overseas FDI by issue of guarantee has also become an important way for Indian companies. The share of financing outward FDI through equities declined from 88.8% in 2000-01 to 73.4% in 2013-14, while share of loans in financing outward FDI from India rose from 10.5% to 26.4% during the

corresponding period. The financing of outward FDI from India through issue of guarantee, which was mere US$ 113 million in 2000-01 rose substantially to US$ 22980 million in 2013-14.

5. The sectoral pattern of outward FDI shows that it has been mainly invested in services and manufacturing sector. Within manufacturing, major sub-sectors which attracted outward FDI from India included agriculture machines and equipments, basic organic chemicals, drugs, medicines and allied products, refined petroleum products, indigenous sugar etc. Similarly, within services sector, a majority of outward FDI has gone into business services, data processing, financial services, architectural and engineering, and other technical consultancy services.
6. The recent trend is showing that outward FDI form India is increasingly flowing to developed countries. This reflects growing confidence of the Indian corporate and availabilities of resources at competitive rates. The off-shore centres in Netherlands, Singapore and Mauritius have been major destinations for outward FDI from India.
7. Outward FDI from India to developed countries have been mainly through mergers and acquisitions, while the mode of entry to developing economies has mainly been through green-field investments. The main reason for mode of mergers and acquisitions in developed economies is that markets are mature there and companies prefer to gain market share through acquisitions rather than green-field investments.
8. One important issue that warrants close monitoring of capital outflows is the implications for domestic investment. There is need to ensure that overseas investment by Indian companies do not dampen domestic investments. There is need to examine the potential impact of rising trend in overseas FDI on domestic investment, growth and employment.
9. The build-up of foreign exchange reserves in last years has supported the initiatives of liberalisation of many of the capital controls including the overseas foreign direct investment from India. Unlimited capital outflows for overseas investment on part of liberalisation of capital controls could have implications for sustainability of India's current account deficit and external debt. In this regard a cautious approach should be adopted.
10. In recent years, there has been rise in the non-fund exposures in the form of issue of guarantees by Indian companies towards the joint ventures and wholly owned subsidiaries abroad. Such substantial issue of guarantees could be a potential risk for Indian banks and companies.
11. The motivations for overseas investment range from genuine business/commercial considerations to taxation benefits which are available to any global investor. This issue should be addressed by providing a transparent policy framework of multilayered structures for outward FDI.
12. There is risk involved overseas business models for a variety of reasons. There is risk of spill over of economic down-turn of foreign economies to domestic economy. Such economic down-turns may adversely impact the financials of the Indian companies with a spill-over effect on the domestic corporate and banking system.
13. The RBI data on overseas direct investments by only captures the actual flows of funds rather than the ultimate destination of investments. The main limitation of the RBI data on joint ventures and wholly owned subsidiaries is that it depicts only the immediate recipient nations of the investment, many of them merely intermediate without having any operations. Steps should be taken in this regard. Establishment of separate institution could serve this purpose along with monitoring and supervision of outward overseas investment from India.
14. The real GDP growth and the government effectiveness in host countries seem main determinants of choices of destination for outward FDI from India.

The analysis indicate that India companies prefer making outward foreign direct investments in the economies where chances of economic growth are better and government is effective in controlling corruption and malpractices. Distance between host economy and India, trade openness of host country and FDI stock in host economy also seem little bit effective in determining the location choices of outward foreign direct investment of Indian companies. It seems that inflation rate in host economy is not considered at all while deciding the location of outward foreign direct investment from India. These findings support the conclusion drawn by Fung and Garcia (2012) that Indian investments are attracted to less corrupt economies with better rule of law while Chinese investments are attracted to more corrupt economies.

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Appendix 1

Descriptive statistics of Data

Statistics	ODI	DIS	FDS	RGR	GOE	INF	TOP
Mean	496.98	6417.3	532444	1.99	1.15	2.89	117.4
Median	121.5	6362	332587	1.95	1.46	2.55	77.2
Max	5098	14350	3929073	15.2	2.30	11.8	447.1
Min	0	1429	1300	-5.6	-0.80	-1.3	24.80
Std. dev.	870.4	3315.6	740996	4.21	0.74	2.48	105.54
Skewness	3.00	0.87	2.90	0.21	-0.94	1.20	1.72
Kurtosis	13.52	3.27	12.37	3.01	2.911	5.30	4.93
Jarque-Bera	538.1	11.38	445.3	0.62	13.0	40.6	57.4
Probability	0.00	0.00	0.0	0.73	0.00	0.00	0.00
observations	88	88	88	88	88	88	88

Appendix 2

Correllogram

Variable	ODI	DIS	FDS	GOE	INF	RGR	TOP
ODI	1.000	-0.124	0.135	0.223	0.025	0.197	0.301
DIS		1.000	0.444	0.321	-0.272	-0.390	-0.282
FDS			1.000	0.324	-0.209	-0.030	-0.056
GOE				1.000	-0.611	-0.322	0.446
INF					1.000	0.324	-0.047
RGR						1.000	0.100
TOP							1.00