Foreign Acquisitions by Indian Multinational Enterprises: A Test of the Eclectic Paradigm

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Abstract

Since the turn of the century India has become the second fastest growing economy in the world. Indian multinational enterprises have increasingly been engaged into acquisitions of foreign firms, in particular in developed economies. While well accepted frameworks such as Dunning's eclectic paradigm were developed in the context of successful Anglo-American firms, there has been no attempt as yet to investigate their explanatory power in the context of mergers and acquisitions by emerging country multinationals. This paper analyses recent trends and patterns in India's outward investment abroad over the period 2000-2007 and identifies their determinants in the context of the eclectic paradigm and the investment development path.

1. Introduction

In less than two decades India has become the second fastest growing economy in the world after China. India has stood out among other developing countries of Asia not only because of recent significant increases in inflows of foreign direct investment (FDI) but also as a result of its potential to be a large outward investor (UNCTAD, 2004) with annual outflows averaging more than US$ 13 billion in recent years. Internationalisation of Indian multinational firms (MNEs), historically undertaken through greenfield investments in the period that preceded gradual liberalisation of India's economy in 1991, has increasingly taken place through cross-border mergers and acquisitions (M&As) since the late 1990s.

This study gains importance from the arguments that the nature, motives and trajectory of internationalisation pursued by MNEs from emerging economies like India have remained a fairly neglected topic. Very little is known about the motives and strategies of these firms as compared to MNEs from developed economies (Kumar, 2006; Bonaglia et al., 2006). It is therefore of crucial importance to examine internationalisation strategies of firms from emerging countries and seek to match their strategies with the concepts and approaches developed under well-established frameworks. Using panel data on foreign acquisitions by Indian MNEs over the period 2000 to 2007 this study is, to our knowledge, a first comprehensive attempt to test well established frameworks such as Dunning's eclectic paradigm (Dunning, 1977, 1981) in the context of OFDI by Indian MNEs.

The focus of this study is on the determinants of FDI through foreign acquisitions and the extent to which established theoretical frameworks of the MNE can explain FDI from emerging countries like India. The remainder of the paper is organised as follows: Section 2 highlights recent trends and patterns in OFDI by Indian MNEs. Section 3 provides a review

of the theoretical frameworks and discusses the extent to which these apply to the case of emerging countries like India. In this section, we introduce country-specific sources of ownership advantages (CSAs) for Indian MNEs. Various hypotheses are framed in Section 4 and Section 5 highlights our modelling strategy. Results and interpretation are discussed in Section 6.

2. Trend and Patterns of Foreign Acquisitions by Indian Firms

Mergers and acquisitions have become Indian MNEs' preferred mode of entry in foreign markets. According to Thomson One Banker dataset, foreign acquisitions by Indian firms have grown significantly both in value and number, especially since 2003. The annual average value of these foreign acquisitions over the last four years amounted to US$ 13 billion (Figure 1). However, the value of these acquisitions tends to be under-estimated as a result of the non-disclosure of the amounts involved in more than 50 per cent of acquisitions.

Figure 1: Foreign Acquisitions by Indian MNEs, in Number and Value, 2000-2007
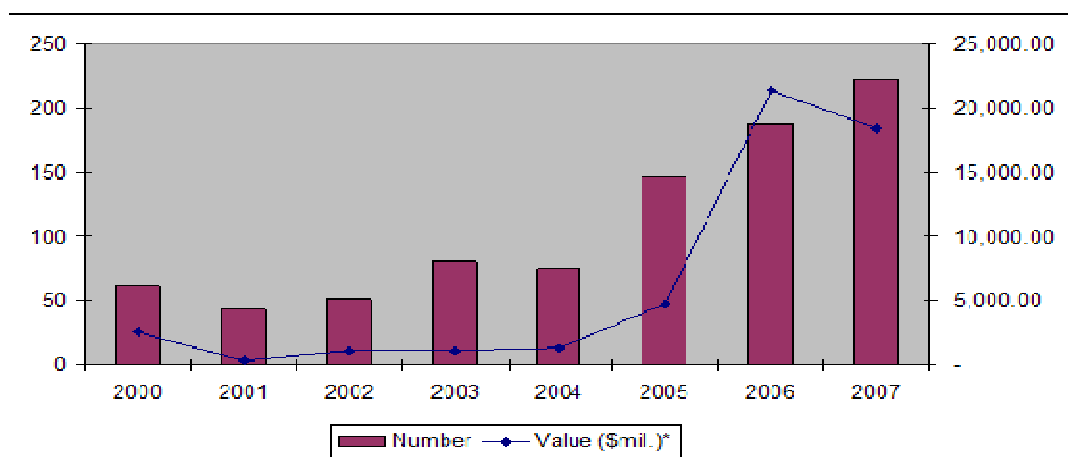
Source: Author's calculations based on Thomson One Banker database.

The concentration of such acquisitions in highly competitive and mature markets of the UK and the USA is striking (Figure 2). According to Thomson One Banker, 866 acquisitions of foreign firms were made by Indian firms in the period 2000 to 2007 of which around 40 percent took place in the UK and the USA. In terms of the value of these acquisitions, these two countries accounted for 54 percent of the total value of all publicly announced acquisitions over the period.

Figure 2: Number of Foreign Acquisitions by Indian MNEs by Host Region, 2000-2007
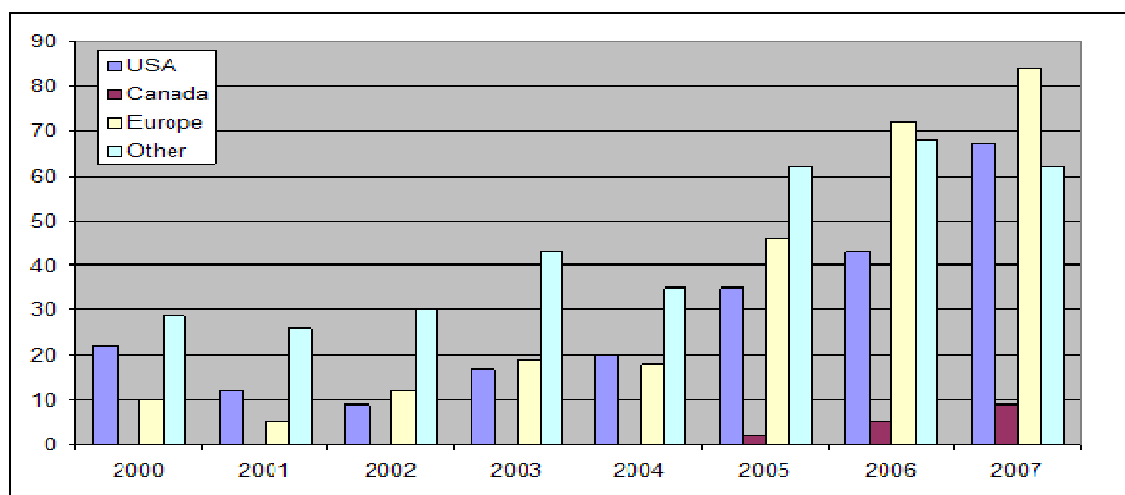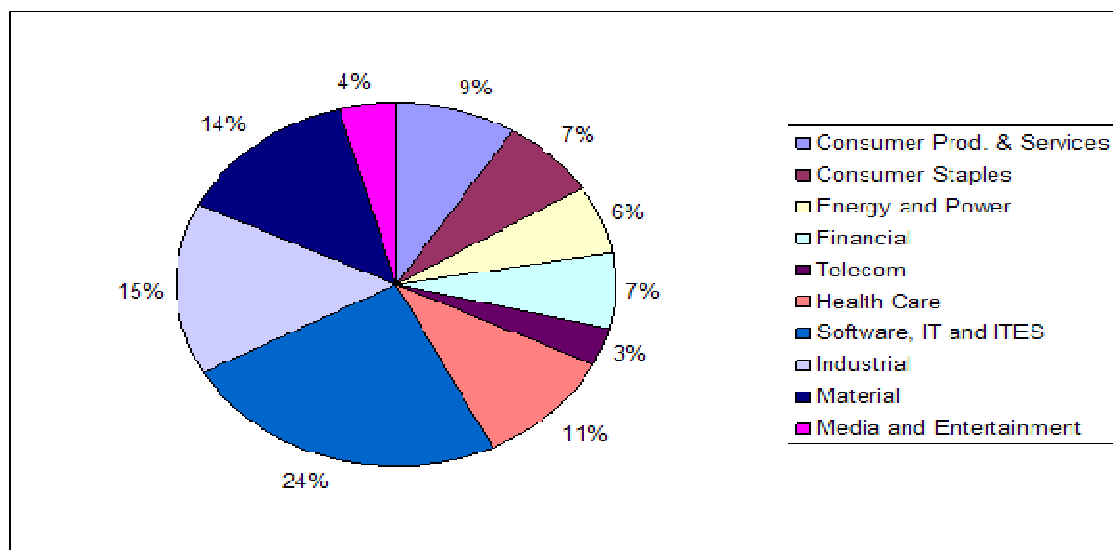

Source: Author's calculations based on Thomson One Banker database.

This pattern is in sharp contrast with the pre-liberalisation period when a similar proportion of Indian OFDI targeted less developed countries (Lall, 1983). While developed countries represent centres for knowledge assets (Pradhan, 2007) for resource- and strategic asset-seeking FDI they also provide Indian MNEs with access to large and developed markets, marketing and distribution channels for well-established brands and wider product portfolio. In addition, developed-country markets are generally mature markets typically served by

MNEs, and this may create incentives for Indian firms to use acquisitions, as opposed to greenfield investments as preferred entry mode.

The sectoral breakdown of these acquisitions reveals the significance of the skill-intensive industries such as high-tech (software in particular) as well as the industrial, chemical and healthcare industries, accounting all together for 52 percent of the number of acquisitions across the period (Figure 3). In particular, non-financial services overtook manufacturing as the leading outward investor sector in the late 1990s, suggesting the services sector may have taken the lead in the mutinationalisation of Indian MNEs. This also reflects the structural shift of the Indian economy towards the services sector which accounts for more than half of the country's GDP (Balasubramanyam & Forsans, 2009).

Figure 3: Industry Distribution of Foreign Acquisitions by Indian MNEs, in percentage of total, 2000-2007

Source: Author's calculations based on Thomson One Banker database.

It is in all these aspects that Indian OFDI differs from that of other emerging countries such as China. While established theoretical frameworks were developed in the context of OFDI by developed country firms, we attempt to examine their application to the context of OFDI by Indian MNEs. The next section introduces these frameworks.

3. Theoretical Frameworks

This section briefly examines the general theory of FDI and attempt to identify home country-specific factors.

3.1 General Theoretical Frameworks

Hymer first conceived the general theory of FDI in 1960, later work by Buckley and Cassons (1976, 1985), Rugman (1981, 1985, and 1996) and Dunning (1977, 1981) formalised the principles of FDI. Accordingly, FDI theory is based on the foundation of imperfection, which is of two types: 1) structural type i.e., market imperfection and 2) cost-type i.e., transaction cost. Structural or market imperfections arises due to existence of advantages (Kalfadellis and Gray, 2002). Advantages can either be country- specific (CSAs) or firm-specific (FSAs). In this paper we discuss the CSAs of Indian firms arising from home country-specific factors such as institutional changes in the form of gradual liberalisation of the economy, domestic capital market and cultural similarities with host countries. These advantages allow MNEs to undertake cross-border expansion by internalising market imperfections. Cost-type imperfections arise from the presence of economic friction during the process of exchange (Williamson, 1981). Transaction costs can be either *ex-ante* (for example, searching cost, negotiation cost, and contracting cost) or *ex-post* (such as enforcing

cost, and coordination cost) to the transaction. These costs are normally inherent and are exogenous to the firm (Hosseini, 2005). Transaction costs in the context of cross border MNE activity became the basis of the Internalisation theory which asserts that MNEs internalise transactions as long as the benefits outweigh costs.

Dunning's eclectic paradigm (Dunning, 1977, 1981) is generally considered as a well-established framework of internationalisation in the literature of international business (Stoian and Filippaios, 2008; Buckley and Hashai, 2008, Narula, 2006). It postulates that outward direct investment results from the existence of ownership, location and internalisation advantages. Having been developed in the context of successful Anglo-American firms in possession of large resources and ownership advantages some authors have argued it may not apply to that of emerging country MNEs (Mathews, 2006, Aykut 2006) endowed with a different set of ownership advantages. Kumar, while analysing the determinants of OFDI from India using a panel dataset covering 4,271 Indian manufacturing firms, found evidence of advantages residing in accumulated production experience; cost effectiveness, and the ability to adapt imported technology and differentiate products (Kumar, 2006).

The eclectic paradigm postulates that OFDI results from the existence of ownership, location and internalisation advantages and the dynamic relation between home country's structural changes and the economic development brings about a change in them. Thus, inward and outward FDI and the level of country development are systematically related and this is the core of Investment Development Path (IDP) theory. At the early stages of development

vertical or resource-seeking FDI tends to take place even though market conditions and local infrastructure may be inadequate. Over a period of time, host country firms learn by doing, develop firm-specific assets, engage in OFDI and evolve themselves as global firms (Dunning, 1981, 1986, 1988 Dunning and Narula, 1996, Caves, 1996).

3.2 Drivers of Indian Outward Direct Investment

We argue in this paper that Indian firms have a different set of CSAs which originates form changes in the institutional factors at home country, state of the domestic capital market and cultural proximity with host countries. In the following subsections we will argue how these factors impart CSAs to Indian firms.

3.2.1 Institutional Factors

Studies in the field of international business (Kogut and Singh, 1988; Peng, 2002; Scott, 2002; Meyer and Nguyen, 2005; Wright et. al., 2005) have explored the impact of institutional factors on FDI decisions. Institutional factors can either act as barriers to foreignness or as a facilitator for FDI. Firms mould their OFDI strategies according to changing institutional frameworks. Government support, in the form of subsidies, easy and simple norms of raising foreign funds can promote foreign investment by offsetting ownership and locational disadvantages abroad (Aggrawal and Agmon, 1990). However, bureaucratic controls, long administrative procedures, quotas, licences and approvals for capital outflows can affect negatively the flow of foreign investment.

Structural or institutional development is implicit in the development of a country. Therefore, the institutional fabric and the degree of structural transformation can influence

and determine OFDI by domestic firms (Lall, 1996; Duran and Ubeda, 2005; Buckley, et. al. 2007). India's outward investment policy was gradually liberalised in the mid-1990s, but it is in the post-2000 period that it reached significance. In a recent FICCI study quoted in Nayyar (2008), FICCI observed that the liberalisation of the policy regime for outward investment in 2005 which allowed Indian firms to invest in entities abroad up to 200 per cent of their net worth in a year coincided with a sharp rise in cross-border acquisitions. It can be observed from Figure 1 and Table 3 that further liberalisation in 2007 which raised overseas investment limit to 400 per cent of net worth in a year, also coincided with the largest number of acquisitions accounting for a value of US$ 18.3 billion compared to US$ 4.7 billion in 2005.

3.2.2 Domestic Capital Market

FDI flows are also very strongly related to source country stock market as high stock valuations at home make financing cheaper by reducing the cost of capital (Baker et. al., 2008). Stock market valuations were also found to have significant explanatory power for US investments abroad (Barrow, 1990) as MNEs make extensive use of their internal capital market to finance FDI projects (Herzer, 2008). The association between stock market valuations and FDI is a very strong one. As Baker puts it, "the effect of source country valuations is stronger, in statistical terms, than any other determinant of FDI that we study, and to our knowledge may be the strongest effect on FDI yet documented in the literature. This relationship is consistent with the cheap finance story" (Baker et al., 2008, pg. 22). However, low market valuations in the host country make acquisitions cheaper and this

should attract FDI inflows. However, there is no evidence that cross-border M&As are attracted by low target valuations (Baker et. al, 2008).

India's capital market remained buoyant especially during the period 2003 to 2007 with significant inflows of global portfolio investments. These conditions have enabled firms to raise equity from both primary and secondary markets. Figure 4, also suggests that Indian firms raised most of the capital in India during this period and this also coincided with increasing levels of cross-border acquisitions by Indian MNEs. Thus, it is likely that such this capital might have been used to finance overseas mergers and acquisitions.

Figure 4: Capital Raised by Indian Companies within India, in INR billion and the Bombay Stock Exchange Index (Sensex)
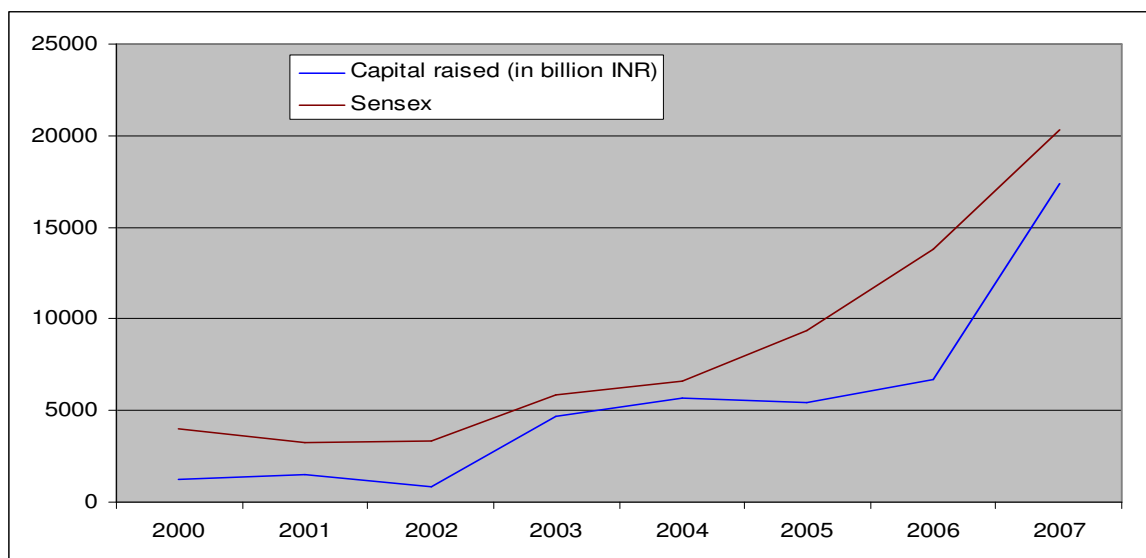
Source: EPW Research Foundation (2008) and Bombay Stock Exchange (2008)

3.2.3 Cultural Factors

The cultural distance between home and host countries is presumed to play an important role in the decision of MNEs to conduct OFDI abroad (Kogut and Singh, 1988; Li and Guisinger, 1991; Barkema et al., 1996, O'Grady and Lane, 1996, Evans et al., 2000). India is culturally close to Western countries, in particular the USA and the UK on account of English proximity and Britain's colonial rule. These two factors are important ones in light of both countries accounting for a significant share of Indian acquisitions abroad. Another advantage for Indian companies is the vast number of non-resident Indians (NRI) overseas. According to the national census surveys Indians are one of the major minority ethnic groups in various countries such as the UK, USA, Canada, and Singapore. The Indian diaspora provides a stream of skilled labour and their cultural affinity to Indian outward investors is likely to be a factor in the choice of location of Indian firms venturing abroad (Balasubramanyam and Forsans, 2009). The Uppsala model of internationalisation suggests gradual internationalisation, with the initial investments in counties which shares similar cultural with home country or where relational assets in the form of personal and professional networks of people (Tschang 2001; Dunning, 2002).

Having identified the source of country-specific advantages of Indian MNEs the next Section will seek to formulate hypotheses derived from theory.

4. The Determinants of Foreign Acquisitions by Indian multinationals

The various hypotheses postulated are categorically created; first on location and internalisation advantages followed by hypotheses on country-specific advantages.

4.1 Location and Internalisation Advantages

The nature of host countries' locational advantages partly depends on the motivation for foreign investment through acquisitions while internalisation advantages depend on various factors affecting transaction costs.

4.1.1 Market Seeking FDI

Developed countries provide Indian MNEs with well developed and mature markets and access to marketing and distribution channels. Acquisitions allow for speed of entry and ownership of well-established brands, marketing skills and marketing distribution networks overseas (Pradhan and Abraham, 2005). Brand building is one of the major desires of Indian companies when investing abroad (Sauvant, 2005). We therefore hypothesise the following:

Hypothesis 1: The number and the value of foreign acquisitions are positively correlated with a host economy's per capita GNIPC.

4.1.2 Resource Seeking FDI

During 2000 to 2007, Indian firms acquired 168 foreign companies, or 20 percent of India's total number of foreign acquisitions for seeking resources. Some were motivated by securing access to inputs to sustain the growth of the Indian economy as illustrated by the acquisition of Russia's Sakhalin and Sudan's Greater Nile by ONGC and the USA's General chemicals by Tata chemicals in 2008. Internalisation theory asserts the importance of equity-based control in the exploitation of natural resources (Buckley et. al., 2007) made possible by acquisitions. Thus, we hypothesise the following:

Hypothesis 2: The number and the value of foreign acquisitions are positively correlated with host country endowments of natural resources.

4.1.3 Asset-Seeking FDI

India is a knowledge-based economy and foreign acquisitions by Indian firms seem to have been directed at the acquisition of knowledge and technology to complement their FSAs. Pradhan argues many software companies from India with ownership advantages might have moved abroad to acquire further knowledge, skill and technology that were not available at home (Pradhan, 2007). There are various examples of acquisitions, especially in knowledge-based industries such as software, business process outsourcing and the pharmaceuticals sectors where such acquisitions took place. Knowledge-based assets can be proxy by the number of patents, copyrights and trademarks within the host economy. Thus, we hypothesise that:

Hypothesis 3: The number and the value of foreign acquisitions are positively associated with host country endowments of knowledge-based assets.

4.1.4 Political risk in the host economy

Empirically, FDI is sensitive to and inversely correlated with political risks in host countries (Harms, 2002). Internalisation theory suggests that countries with high political risks would be served by arm length-servicing modes, e.g., exporting, licensing, and outsourcing (Buckley and Casson, 1981, 1999; Delios and Henisz, 2003) because FDI involves a higher degree of a firm's commitment and the existence of sunk costs. However, recently scholars have found that feeble institutional structure and the instability may be attractive to some

firms because of their ability and experience to work in such environments (Fisman and Khanna, 1998). Indian firms have experience of operating within home country environment which does not offer good socio-economic conditions, stable government and have internal or external conflicts. Thus, it is likely that political risk in the host country may not be a significant factor in foreign acquisitions. However, we hypothesise:

Hypothesis 4: The number and the value of foreign acquisitions are negatively associated with host countries' political risk.

4.1.5 Corporate Tax

FDI theory recognises that the decision to locate foreign investments may be shaped by the nature of taxation provisions in host countries and their impact on the returns of investment projects (Swenson, 1994). Various time-series studies found a positive correlation between higher after-tax returns and the amount of FDI (Desai et. al., 2004). Corporate tax rates play an important role in the location choices of MNEs as firms prefer to locate activities in low statutory tax rate countries (Grubert and Slemrod, 1998). We therefore hypothesise that

Hypothesis 5: The number and the value of foreign acquisitions by Indian multinationals are negatively associated with the host country corporate tax rate.
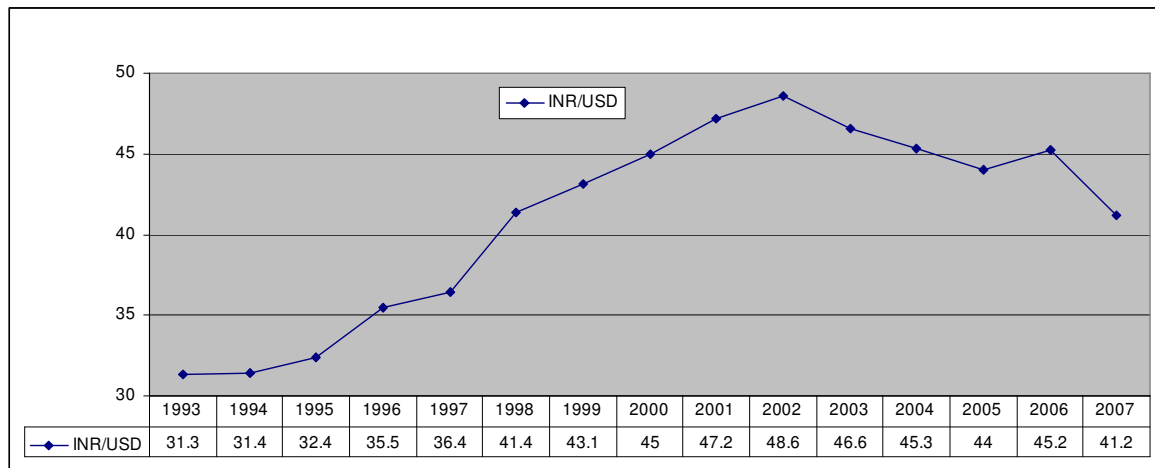
4.1.6 Exchange Rate

The appreciation of home country currency discourages exports and encourages overseas investment. Many studies (Aliber, 1970, Stevens, 1993, Blonigen, 1997) cite exchange rate as a critical determinant of FDI. The strengthening of the Indian rupee in recent years against the US dollar made valuations of target companies abroad attractive, enabling a surge

in foreign acquisitions by Indian firms. The exchange rate of the Indian rupee against the US

dollar, which peaked in 2002 at 48.6 INR/USD appreciated by more than 15 per cent by 2007

(Figure 5). This may impact on the volume of foreign acquisitions. Thus, our hypothesis is:

Hypothesis 6: The number and the value of foreign acquisitions are negatively associated

with depreciation of USD against INR.

Figure 5 : Foreign Exchange Rate of Indian Rupee against USD

	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
INR/USD	31.3	31.4	32.4	35.5	36.4	41.4	43.1	45	47.2	48.6	46.6	45.3	44	45.2	41.2

Source: The Federal Reserve (2008)

4.1.7 Geographical distance

Internalisation theory (Buckley and Cassons, 1981) suggests the importance of geographical

distance in OFDI decisions. Higher the geographical distance more will be the transaction

cost. A physical distance variable is also needed to complement the cultural distance

variable, to isolate its effect (Buckley et al., 2007). Thus, flow of FDI should negatively

relate to the geographical distance. Therefore, we hypothesise:

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Hypothesis 7: The number and the value of foreign acquisitions are negatively associated with geographic distance between the capitals of home and host countries.

4.1.8 Openness of Host Economy

Openness of an economy for trade and investment is an important variable in attracting FDI (Chakrabarti, 2001) - the more open a host country the larger the number of acquisitions it may attract. Therefore, we hypothesise:

Hypothesis 8: The number and the value of foreign acquisitions are positively associated with openness of the host economy.

4.2 Country-specific ownership advantages

In this subsection we frame our hypotheses for the CSAs introduced in Section 3 which may have explanatory power for the foreign acquisitions.

4.2.1 Inward FDI flows in the Home Country

Capital flows in the form of FDI act as catalysts in the economic activities and growth of the home country. The IDP suggests that inward FDI boosts economic growth which in turn increases outward FDI by domestic firms (Dunning, 1981, 1986, 1993b; Dunning and Narula, 1996, Barry et al., 2003). Duran and Ubeda (2001) argued that Indian OFDI is at the second stage in IDP although India is characterised by large FDI outflows relative to the inflows for a country at its development stage. However, the IDP theory suggests that inward FDI leads to FDI outflows. Thus, we hypothesise:

Hypothesis 9: The number and the value of foreign acquisitions is positively associated with India's inward FDI flows.

4.2.2 Institutional Changes in the Home Country

Institutional changes are fundamental changes in an economy that might affect the investment patterns of firms. Changes in institutions of a country brought together with economic development may affect home country's OFDI (Dunning, 1981, 1986, 1993b; Dunning and Narula, 1996). Thus, fundamental changes in the outward investment policy of India might be enabling factors in foreign acquisitions by Indian MNEs. Key policy changes in the evolution of outward FDI are presented in Table 3. A major liberalisation in outward investment policy took place in the year 2003, when companies were allowed to invest 100 per cent of their net worth abroad. We therefore hypothesise the following:

Hypothesis 10: The liberalisation of India's overseas investment policies from 2003 is positively associated with the foreign acquisitions of Indian MNEs.

4.2.3 Domestic Capital Market

There is an inverse relationship between a firm's stock valuation and its cost of capital. As mentioned earlier in Section 3.2.2, high valuations on the Indian stock market coincided with high levels of equity raised by Indian firms in home country (See Figure 4) which coincides with the increasing M&A activities. These funds might have been used to finance overseas mergers and acquisitions. Thus, it has been hypothesised that:

Hypothesis 11: The number and the value of foreign acquisitions are positively associated with stock market index.

4.2.5 Cultural Distance with the Host country

Most of the studies in the international business literature make use of the Kogut and Singh's (1988) composite index on cultural distance. Kogut and Singh cultural distance index is based on the Hofstede's (1980, 1983, 1991, 2003) empirical framework of national dimensions of culture, such as power distance, uncertainty avoidance, individualism versus collectivism and masculinity versus femininity.

Though, Hofstede's cultural dimensions and Kogut and Singh's cultural distance composite index is not free from limitations (Sodergaard, 1994; Shenkar, 2001; Harzing, 2003; Shenkar et al. 2008; Chapman et al. 2007). Yet, Hofstede's framework is generally well accepted to become the most quoted in its field (Sondergaard, 1994; Bond, 1988). Kogut and Singh's index or its modified version is used most often in various studies (e.g., Kale, 1991; Benito and Gripsrud, 1992; Agarwal, 1994; Barkema et al., 1996). Kougt and Singh (1988) composite index on cultural distance is based on a formula which takes the difference between the index scores of the different countries relative to USA. The algebraic representation of the Kogut and Singh index (1988) is as follows:

$$CD_j = \sum_{I=1}^{4} \{(I_{ij} - I_{iu})^2 / V_i\} / 4$$

Where, CD_j = cultural distance of ith country from the United States

I_{ij} = index of the ith cultural dimension and the jth country

I_{iu} = index of the ith cultural dimension of the US as u stands for United Status.

V_i = is the variance of the index of the ith cultural dimension.

Kogut and Singh CD index was computed for each host country with respect to its difference with India to generate a CD index relative to India. We hypothesise:

Hypothesis 12: The number and the value of foreign acquisitions are negatively associated with the host countries value of cultural distance index in relation to India.

4.2.6 Cultural and Language Proximity

It is argued that the ethnic and diaspora networks act as relational assets and constitute firm-specific advantages (Buckley et al., 2007; Dunning and Lundan , 2008). Thus, Indian diaspora should act as a pulling factor for many Indian firms investing abroad. Studies (Tschang 2001; Saxenian et. al., 2002) on Indian expatriates suggest that Indian companies set up business in countries with a large resident population of ethnic Indian. Similarly, the competence of Indians in the English language can also provide advantage to Indian firms in English speaking countries. Thus, the following hypothesis is created.

Hypothesis 13: English speaking countries are positively associated with foreign acquisitions by Indian MNEs.

5. Research Methods

To test our hypotheses we have constructed two models based on two dependent variables, namely the number of foreign acquisitions abroad by Indian firms and the value of these acquisitions over the period 2000-2007. We match the dependent variable (acquisitions both in numbers and value) and all independent variables (such as host country's GDP, political risk, patents applications and so on) to create a panel data set. We transformed both dependent and a set of independent variables into natural logarithms and derived a log-log linear model. Log-log function enables the transformation of non-linear relationship between

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our dependent and independent variables into a linear one. It measures FDI elasticity with

respect to our set of explanatory variables (Crown, 1998). Thus, our models are as follow:

(1) $\text{Ln}(\text{MAValue}_t) = a + b_1 \ln(\text{GNIPC}) + b_2 \ln(\text{RE}) + b_3 \ln(\text{PATENT}) + b_4 \ln(\text{FERATE}) + b_5$
$\ln(\text{CTAX}) + c_1 \ln(\text{FINFDI}) + c_2 \ln(\text{IC}) + c_3 \ln(\text{SENSEX}) + c_4 \ln(\text{DEBIT}) + c_4 \ln(\text{CDI}) + c_6$
$\ln(\text{NRI}) + c_7 \ln(\text{ENG})$

(2) $\text{Ln}(\text{MANo}_t) = a + b_1 \ln(\text{GNIPC}) + b_2 \ln(\text{RE}) + b_3 \ln(\text{PATENT}) + b_4 \ln(\text{FERATE}) + b_5$
$\ln(\text{CTAX}) + c_1 \ln(\text{FINFDI}) + c_2 \ln(\text{IC}) + c_3 \ln(\text{SENSEX}) + c_4 \ln(\text{DEBIT}) + c_4 \ln(\text{CDI}) + c_6$
$\ln(\text{NRI}) + c_7 \ln(\text{ENG})$

The definition and source of each variable in our models are highlighted in Table 2.

Table 2 : Variables and Data Sources

	Variable (General)	Proxies	Expected Sign	Theoretical Justification	Data Source
Dependent Variables	Value of Foreign Acquisitions by Indian firms **(LMAValue)** Number of Foreign Acquisitions by Indian firms **(LMANo)**	Dependent variables			Thomson One Banker
Internalisation and Location Variables	Market Size of Host Country **(GNIPC)**	GDP and Per Capita GDP	+	Market Seeking	World Bank Development Indicator
	Natural Resource Endowment of Host Country **(NRE)**	Ratio of Ore and Metal Exports to Merchandise Exports of Host Country	+	Resource Seeking (Leverage)	World Bank Development Indicator
	Endowment of Knowledge Based Asset of Host Country **(KBA)**	Yearly Patent Registration in Host Country	+	Resource Seeking (Leverage)	World Intellectual Property Organisation
	Political Risk **(POLRISK)**	Host country's political risk rating	-	Transaction Cost	International Country Risk Guide
	Corporate Tax **(CTAX)**	Corporate Tax Rates in Host Country	-	Transaction Cost	OECD: Centre for Tax Policy and Administration
	Exchange Rate **(FOREX)**	Host country official annual average exchange rate against dollar	-	Macro Economic Factors	World Bank Development Indicator
	Economy Openness of Host Country **(OPEN)**	Ratio of Foreign Trade to GDP	+	Transaction Cost	World Bank Development Indicator

	Geographical Distance of Host country (GEODIS)	Distance between the capitals of host and home country	-	Transaction Cost	Calculated using www.geobytes.com
Ownership Variables (CSA)	Direct Capital Flow (INFDI)	Inward FDI in home country	+	IDP	DIPP
	Institutional Change or Policy Liberalisation (IC)	Time dummy variable	+	Institutional Factors	Reserve Bank of India
	Domestic Capital Market (SENSEX)	Bombay Stock Exchange Index	+	Special Variable (Ownership Advantage)	National Stock Exchange Of India
	Cultural Distance Index (CDI)	Kogut and Singh CD Index	_	Uppsala Model	Kogut and Singh (1988)
	English Speaking Host Country (ENG)	Binary Code	+	Uppsala Model	Krysstal.Com

5.1 Dataset and Proxies

The Reserve Bank of India does not compile data on cross border mergers and acquisitions. As a result we sourced annual data on foreign acquisitions by Indian firms from Thompson One Banker's M&A database. We tested the database's exhaustive coverage by manually checking all reported acquisitions over the first six months of 2008 and were satisfied our database covered the whole population. Our dataset reveals that 866 acquisitions of firms headquartered in 82 countries took place over the period 2000-2007 by Indian firms.

Our independent variables were sourced from reliable sources as indicated in Table 2.

6. Results and Findings

Tables 3 and 5 present the values of R squares for our models while Table 4 and 6 present the significance of coefficients and collinearity statistics such as VIF and tolerance. Our results are consistent across both models.

6.1 Location and Internalisation advantages at the Host Country

In Section 2 we indicated the strong concentration of India's acquisitions into mature, well developed countries such as the USA and the UK. This inclination has significant market seeking motives (Hypothesis 1). Developed, high income-per-capita countries (GNIPC) provide Indian firms with strong incentives to establish a local presence, e.g. through the size of their market. However, we find that host countries' natural resource (NRE) and knowledge-based assets (KBA) endowment do not have a significant influence on both the value and the number of acquisitions (Hypotheses 2 and 3). Other location factors included political risk and corporate tax (Hypotheses 4 and 5). These were found to be insignificant, maybe as a result of domestic market conditions. The political risk index we used in this study is a composite index that takes into account many different factors such as government stability, socio-economic conditions, investment profile, corruption, law and order, ethnic tensions, democratic accountability etc. India, unlike most developed economies tends to have a poor track record in these areas. Indian MNEs might have gained experience of operating in difficult environments at home, and this may explain the lack of significance in our political risk variable. While theory tends to suggest negative correlation between OFDI and corporate taxation in host countries, our corporate taxation variable (Hypothesis 5) appears to be insignificant. This may be explained by Indian firms engaging into market- or asset-seeking acquisitions abroad rather than minimisation of corporate taxation. Favourable exchange rate (Hypothesis 6) has made valuations of foreign target companies more attractive and the role played by exchange rates appears to be strongly significant. The strengthening of the Indian Rupee against the US dollar appears to have encouraged Indian firms into acquisitions away from home as a result of more attractive valuations of foreign

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companies when expressed in home-country currency. Geographic distance (Hypothesis 7) and the openness of host countries (Hypothesis 8) are not found to be significant. Insignificance of geographic distance testifies the fact that the bitter rivalries in South-Asia region especially among India, China and Pakistan have made this area least integrated (Foreign Commonwealth Office, 2007).

Thus, Indian companies have made market-seeking acquisitions abroad, especially in advanced countries where the valuations of these firms were made more attractive as a result of the strengthening of the Indian rupee.

Table 2 : **Model Summary (Dependent variable : MAValue)**

				Change Statistics				
R	R Square	Adjusted R Square	Std. Error of the Estimate	R Square Change	F Change	df1	df2	Sig. F Change
.460[a]	.212	.193	5.31088	.212	11.311	13	547	.000

a. Predictors: (Constant), LInFDI, LGeoDis, LForex, Eng, LKBA, LCTax, LGNIPC, LPolRisk, LCDI, PolicyLib, LNRE, LTradeGDP, LSensex

Table 3: **Coefficients[a]**

	Unstandardized Coefficients		Standardized Coefficients			Collinearity Statistics	
Model	B	Std. Error	Beta	t	Sig.	Tolerance	VIF
(Constant)	-62.770	14.920		-4.207	.000		
LGNIPC	.131	.061	.132	2.158	.031*	.386	2.589
LNRE	.052	.069	.041	.750	.454	.473	2.113
LKBA	.005	.027	.007	.190	.849	.955	1.047
LPolRisk	.071	.069	.051	1.023	.307	.578	1.730
LCTax	.007	.033	.009	.210	.834	.838	1.193
LForex	-.213	.072	-.122	-2.963	.003**	.855	1.170
LGeoDis	-.158	.398	-.016	-.398	.691	.840	1.190

LlnFDI	1.018	.744	.081	1.370	.171	.413	2.423
PolicyLib	-.783	.884	-.066	-.886	.376	.263	3.809
LSensex	3.829	.994	.327	3.850	.000**	.200	5.009
LCDI	.143	.048	.150	2.994	.003**	.574	1.742
Eng	2.472	.619	.154	3.991	.000**	.964	1.037
LOpen	-.119	.077	-.093	-1.551	.122	.400	2.502

a. Dependent Variable: LMAValue

** Significant at 1 %; * significant at 5%

Table 4 :**Model Summary (Dependent variable: MANo)**

R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics				
				R Square Change	F Change	df1	df2	Sig. F Change
.441[a]	.195	.176	4.99743	.195	10.186	13	547	.000

a. Predictors: (Constant), LInFDI, LGeoDis, LForex, Eng, LKBA, LCTax, LGNIPC, LPolRisk, LCDI, PolicyLib, LNRE, LTradeGDP, LSensex

Table 5: **Coefficients**[a]

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.	Collinearity Statistics	
	B	Std. Error	Beta			Tolerance	VIF
(Constant)	-38.546	14.039		-2.746	.006		
LGNIPC	.096	.057	.104	1.679	.094*	.386	2.589
LNRE	.061	.065	.052	.932	.352	.473	2.113
LKBA	-.003	.025	-.005	-.116	.908	.955	1.047
LPolRisk	.091	.065	.070	1.395	.164	.578	1.730
LCTax	.006	.031	.008	.191	.849	.838	1.193
LForex	-.180	.068	-.110	-2.663	.008**	.855	1.170
LGeoDis	-.498	.375	-.056	-1.327	.185	.840	1.190
LInFDI	.115	.700	.010	.165	.869	.413	2.423
PolicyLib	-.351	.832	-.032	-.422	.673	.263	3.809
LSensex	3.701	.936	.340	3.955	.000**	.200	5.009
LCDI	.139	.045	.156	3.080	.002**	.574	1.742
Eng	2.130	.583	.143	3.655	.000**	.964	1.037
LOpen	-.113	.072	-.095	-1.563	.119	.400	2.502

a. Dependent Variable: LMANo

** Significant at 1 %; * significant at 5%

6.2 Country Specific Advantages at the Home Country

In order to evaluate country-specific sources of advantages we considered three sets of determinants: the inward flow of foreign direct investment (InFDI); the liberalisation of India's outward investment policy (PolLib); Jump in the domestic capital market (SENSEX) and cultural factors such as cultural proximity (CDI) and language (ENG) proximity between home and host countries. The IDP theory suggests that inward flows of FDI boost outward flows of FDI. Contrary to theory, India's inward FDI flows (Hypothesis 9) are not significant in explaining outward FDI through M&As. This may be because India is untypical of most other developing economies with large FDI outflows in recent years relative to the size of its inflows for a country at the early stages of its development path. Indeed, FDI outflows surpassed inflows in 2007. Institutional changes (Hypothesis 10) were not found to be significant either unlike our domestic capital market variable (Hypothesis 11) as increases in the stock market index might have enabled Indian firms to fund foreign acquisitions.

Among the cultural variables under investigation, both cultural distance (Hypothesis 12) and language proximity with English speaking countries (Hypothesis 13) were found to be significant. Thus, cultural proximity matters to Indian MNEs.

Conclusion

This paper is a first attempt to model the determinants of Indian OFDI through mergers and acquisitions with the view to investigate the extent to which these can be explained in the

context of the eclectic paradigm. Using a panel dataset on foreign acquisitions by Indian MNEs in 82 countries over the period 2000-2007 we tested a number of hypotheses. We find that Indian OFDI through cross-border acquisitions have both conventional and idiosyncratic dimensions. While we found that Indian acquisitions abroad were primarily motivated by market-seeking purposes, we could not find evidence of resource and strategic asset-seeking FDI. The role of exchange rate fluctuations and that of cultural and language factors were also found to be important determinants of these acquisitions which appear to have been funded on the back of rising corporate valuations on India's stock market over the past decade. By contrast we could not find support for the implications from the investment development path – this can be explained by India's untypical "leapfrog" development model which evolved from an agriculture-based economy into a services-based one, largely bypassing manufacturing.

This first attempt at applying well accepted frameworks to the case of outward foreign investment by emerging country multinational needs refining. While we expected policy liberalisation to have some explanatory power our results did not confirm our hypothesis. This may be as a result of our modelling strategy which will need reconsidering.

Appendix

Table A1 : Correlation Matrix

	LNRE	LKBA	LPol.Risk	LCTax	LForex	LGeogDis	LCDI	LSensex	PolicyLib	Eng	LTradeGDP	LGNIPC	LlnFDI
LMANo	.131	.021	.140	.078	-.056	.008	.217	.329	.272	.145	.018	.130	.256
LMAValue	.131	.032	.124	.084	-.069	.043	.214	.343	.275	.159	.014	.139	.295
LNRE	1.000												
LKBA	.079	1.000											
LPolRisk	.506	.088	1.000										
LCTax	.322	.078	.160	1.000									
LForex	.279	.025	.316	.063	1.000								
LGeogDis	.268	.130	.101	.150	.025	1.000							
LCDI	.495	.067	.557	.258	.180	.164	1.000						
LSensex	-.033	.064	-.011	.003	-.028	.001	-.007	1.000					
PolicyLib	-.015	.065	-.004	-.090	-.030	.000	-.003	.851	1.000				
Eng	.082	-.065	-.055	.035	.005	.081	.057	-.002	.000	1.000			
LTradeGDP	.504	-.060	.316	.136	.284	-.089	.315	-.133	-.084	.059	1.000		
LGNIPC	.545	-.024	.365	.204	.245	-.009	.452	-.024	-.011	.031	.734	1.000	
LlnFDI	-.043	.022	-.008	-.027	-.019	.001	-.005	.762	.665	-.001	-.155	-.038	1.000

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