

Outbound Foreign Direct Investment from China and India: The Role of Country-specific Factors¹

Khanindra Ch. Das

Rajiv Gandhi Indian Institute of Management
Mayurbhanj Complex, Nongthymmai
Shillong
kchdas@gmail.com

Nilanjan Banik

Mahindra Ecole Centrale
Bahadurpally, Hyderabad

Chinese and Indian enterprises have been increasingly involved in international business thereby attracting global attention since the turn of the 21st century. This article examines outbound investment experiences of Chinese and Indian multinationals and compares and contrasts the investment development trajectory for both the countries. The comparisons and contrasts are made with respect to government policy, motivations for outbound investment, financing of investment, success rate in overseas acquisition, sectoral composition, characteristics of multinational enterprises (MNEs) and the challenges and impact of such investments in the light of differences in economic and institutional parameters between the two countries. It can be observed that there are more differences than similarities in the trajectory of outbound investments by Chinese and Indian enterprises. These differences arise due to the economic and institutional structure and the development path chosen by the two countries. Due to the differences between Chinese and Indian economic development trajectories, which are unique in many ways, it is not meaningful to make a straightforward comparison of outbound foreign direct investment (FDI) experience of the two countries. Nevertheless, the main differences with regard to outward investment by Indian and Chinese enterprises can be observed in areas such as the degree of involvement of the public sector enterprises, financing of overseas investments, success rate of proposed mergers and acquisitions (M&A), sectoral composition of

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such investments, investment motives and so on. Various challenges facing outward FDI from China and India are highlighted, some of which could be addressed by specific economic and institutional reforms. The tale of the two countries examined in this article taken together contains important insights for emerging country enterprises and governments on the challenges and opportunities of global business.

Keywords: China, India, mergers and acquisitions, outbound FDI, corporate governance, economic reforms

Whether you think globalisation is a ‘good thing’ or not,
it appears to be an essential element of the economic history of mankind.

(The Economist 2013)

China and India have received special attention in the international arena, from many perspectives, in the light of their regional and global economic emergence in recent decades. China became the second-largest economy in the world replacing Japan in 2009, and maintained its position thanks to its spectacular economic growth, and it is only a matter of time before it occupies the first place (Jorgenson and Vu 2013; OECD 2012; *The Economist* 2011). On the other hand, India’s economy was ranked 10th largest in 2012 as per National Accounts Main Aggregates Database of the United Nations Statistics Division. China and India are also the two most populous countries in the world. In 2012, China had a population of 1,350.7 million and that of India was 1,236.7 million (World Development Indicators: World Bank). Nevertheless, the impressive growth over the last decade and continuation of the same in the near future, through demographic dividend and large human capital base, have the potential to lift India to the ranks of the top five economies in the world.

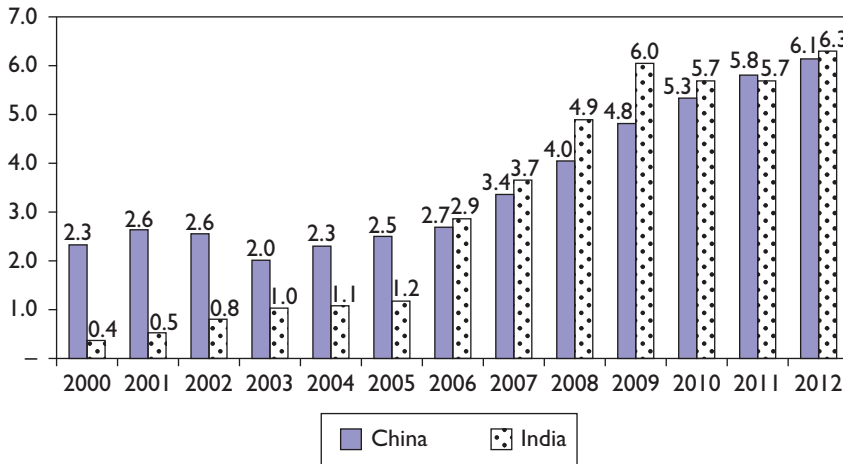
The achievement in exports and inward foreign direct investment (FDI) has been commendable for both the countries, more so in the case of China. However, both the countries are becoming a source of capital as they are increasingly engaged in outward FDI. China’s outward investment is driven by current account surplus, whereas that of India is taking place despite the current account deficits. Nevertheless, both countries possess huge amount of international reserves although accumulated differently.²

China’s share in world outward FDI flows was a meagre 0.07 per cent in the year 2000, which increased to 1.48 per cent in 2006 and then to 6.52 per cent in 2012. Outward investment from India was sporadic in the earlier decades. Nevertheless, in the last decade it increased steadily. India’s share in total world FDI outflows increased from 0.04 per cent in 2000 to 1.00 per cent in 2006 and reached 1.37 per cent in 2009, and then shrank somewhat to 0.63 per cent in 2012. Furthermore, outward FDI stock as percentage of gross domestic product (GDP) in India rose from 0.4 per cent in 2000 to 6.3 per cent in 2012. In the case of China, the same increased from

² At the end of 2010, China had a foreign exchange reserve of US\$ 2,847 billion and that of India was US\$ 268 billion (International Financial Statistics: IMF).

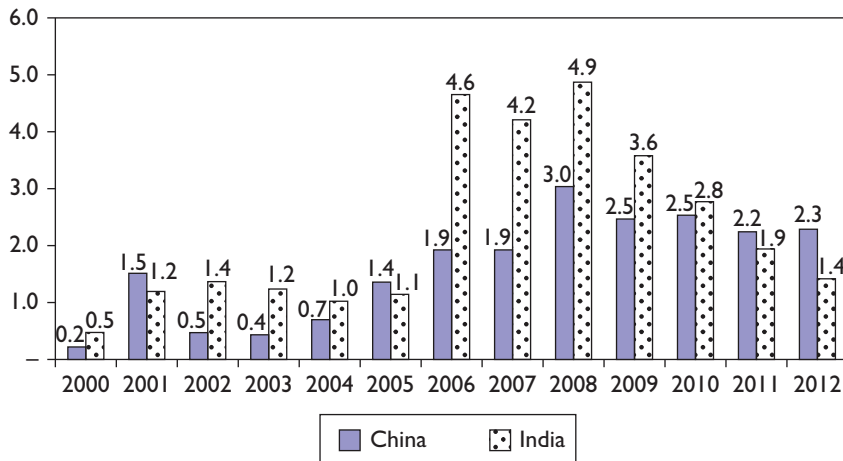
2.3 per cent in 2000 to 6.1 per cent in 2012 (Figure 1). Similarly, outward FDI flows as percentage of gross fixed capital formation in India increased from 0.5 per cent in 2000 to 1.4 per cent in 2012, whereas the same went up from 0.2 per cent in 2000 to 2.3 per cent in 2012 in the case of China (Figure 2).

Figure 1
Outward FDI Stock of China and India (Percentage of GDP)



Source: Authors' compilation from UNCTAD (World Investment Report, 2014).

Figure 2
Outward FDI Flows of China and India (Percentage of Gross Fixed Capital Formation)



Source: Authors' compilation from UNCTAD (World Investment Report, 2014).

Outbound investment is characterised as a natural phenomenon in the process of economic development and globalisation. Firms try to explore the specific advantages they possess by expanding their operations to the international market. They also acquire advanced technology, managerial skills and scarce resources in the process. Outbound FDI is therefore a natural strategy for firms to explore global markets, which also brings complementary benefit to the outward investing firms as it helps in catching up with international best practices and strengthening their competence. Both Chinese and Indian governments have recognised outbound investment as beneficial for the growth of enterprises and a necessity for enhancing global integration.

There are various modes of outbound investments among which mergers and acquisitions (M&A) and greenfield investments are prominent in the context of emerging countries such as China and India. Overseas acquisition of enterprises by multinationals from India and China has attracted global attention since the turn of the 21st century. Against this backdrop, this article examines the emerging pattern of outbound investment experiences of Indian and Chinese multinationals and compares and contrasts the investment development trajectory for both the countries. The comparisons and contrasts are made with respect to government policy, motivations for outbound investment, financing of investments, success rate in overseas acquisition, sectoral composition, characteristics of multinational enterprises (MNEs), challenges facing such investment and the impact of such investments in the light of differences in economic and institutional parameters between the two countries that led the observed trajectory of outbound investments. Nevertheless, it should be kept in mind that straightforward comparison between Indian and Chinese outbound investments is not easy. Other than large populations, relative poverty and rapid economic growth, the two countries have little in common (Bottelier 2007: 53). Although outward FDI from the two countries has expanded, drawing a comparative picture, as has been attempted in previous studies, is not always meaningful due to differences in the structural and institutional features of the two economies.³ Thus, this article attempts to bring out an overall perspective on the similarities and differences in the trajectory of outward FDI of the two countries by highlighting the contributing factors, political and economic, and the lessons and implications for both the economies as well as for other emerging countries.

The rest of the article is organised as follows. The first section gives an economic and institutional background of the two economies through a discussion of the economic and institutional reforms undertaken in the two countries. Some features of outward

³ For an overview of internationalisation of Chinese and Indian firms, see Athreye and Kapur (2009); also see Kumar and Chadha (2009) for steel industry; Duysters et al. (2009) for comparison of Haier Group and Tata Group; Niosi and Tschang (2009) for software industry; and Rui et al. (2010) for a comparison of selected Chinese and Indian multinational companies (MNCs) such as Nanjing Automobiles, Lenovo, Huawei vs. Maruti, Wipro and Infosys; aggregate outward FDI flows Hong (2011) and Nagaraj (2012); bilateral outward FDI flows Pradhan (2011) and Fung and Garcia-Herrero (2012).

FDI from the two countries are analysed in the next section using data. The following section discusses the factors that prompted outward FDI from the two countries and various other facets. In the conclusion, the article discusses future prospects and challenges facing the two economies in the area of global FDI and the implications for emerging countries' outbound investments.

REFORMS IN CHINA AND INDIA

Economic and institutional reforms in China had started in the late 1970s and early 1980s under the leadership of Deng Xiaoping, and described as 'building of socialism with Chinese characteristics'. The reforms progressed without jettisoning planning.⁴ China's development paradigm has been explained thus by Michael Chibba:

China's stellar economic growth and overall development since the 1980s resulted from its authoritarian, state-led, development paradigm, which is tempered by ideology, culture, economics, and domestic and international politics. But it has been shaped, at least in part, by the very nature of the Chinese dynamics of planning, decision making, implementation, review, and adjustment—what some observers refer to as a pragmatic philosophy...economic development in China was assisted by several additional developments (national, regional and global) that included (1) steady inflow of foreign direct investment to tap into its absolute advantage—a large pool of low cost labour; (2) favourable conditions to support increased global capital mobility; (3) consistent current account surpluses; (4) an undervalued yuan (renminbi); (5) segmentation in global manufacturing; (6) trade liberalization; (7) good infrastructure in China; and (8) China's unique but limited market oriented reforms, with the state acting as observer and the ultimate authority. (Chibba 2011: 151)

India embraced a planned economy in the post-independence era that held back development. The strategy of planned economic development emphasised self-reliance and protectionism through industrial policy and the *license raj*,⁵ financial repression and

⁴ This is known as the 'birdcage thesis' by Chen Yun. See Yergin and Stanislaw (1998: 192–213).

⁵ The term *license raj* (or *permit raj*) refers to the industrial licensing policy that existed in India since independence till the early 1990s. Under this regime, firms could manufacture goods only after obtaining government licences. The central government of India has eliminated many of these restrictions through economic reforms starting from 1991. However, the existence of *license raj* at the state level is observed (Athukorala 2009), although it had been largely eliminated at the centre, along with a pervasive *inspector raj*. In view of myriad regulations at the state level, the need for further reforms in the Indian economy has been strongly felt (e.g., with respect to labour, bankruptcy, multiple laws) to promote ease of doing business and to make use of the cheap labour force and labour-intensive industrialisation (Acharya 2009; Lal 2011; Srinivasan 2011).

state ownership of large industries. Inefficiencies rippled through the entire economic system that led to the piecemeal reforms in 1980s. However, the balance of payments crisis in 1991 left India with no option but to liberalise and deregulate the economy in a progressive manner, which brought a window of opportunity for expansion of the private sector that coincided with the rise of globalisation, leading to rapid economic development in the country.

A special institutional feature of Chinese reform is in terms of decentralised experiments and career incentives for the local officials, which facilitated economic development and rural industrialisation in a way that is rather unique. In India, on the other hand, the system is more top-down and leaves few incentives for local officials to perform (Bardhan 2010). Nevertheless, the strength of Indian firms was nurtured through the process of import substitution in the pre-reform era by restricting imports and inward FDI (Kumar 2008).⁶

The post-reforms performance in both the countries has been impressive. India's share in world GDP improved marginally from 3.1 per cent in 1990 to 5.4 per cent in 2010. The per capita GDP more than tripled from US\$ 378 in 1990 to US\$ 1,265 in 2010. China's share in world GDP increased substantially from 3.9 per cent in 1990 to 13.6 per cent in 2010. The per capita income increased more than 10 times from US\$ 341 to US\$ 4,382 during the same period (The BRICS Report 2012: Table 1.1, p. 2). Thus, although India and China were similar in the 1990s in terms of economic size and the level of development, captured by GDP per capita, China outpaced India in both aspects reflecting the differences in the development strategy in the two countries.

Under China's open-door economic policy adopted in 1978, it established special economic zones in coastal provinces. Since then the country has attracted a considerable amount of foreign capital to become the largest recipient of inward FDI in the following decades. Increase in inward FDI is considered as one of the greatest drivers of economic growth in China. China's FDI receipt, mostly in the manufacturing sector, contributed to exports, current account surplus and official foreign exchange reserve (Sun 2012; Wu et al. 2013; Zhang and Felmingham 2001). This in turn helped China in navigating the transition to outward FDI. However, the number of outward FDI proposals were just a few till the early 1990s, and were concentrated in a few sectors and countries that were geographically close by. Nevertheless, the build up of industrial capacity in the Chinese economy had led to the realisation of the potential benefits of outward FDI. As a result, since the 1990s, the Chinese government has facilitated the process of outward FDI, which was boosted further

⁶ Out of India's 46 billionaires in 2012, 20 had drawn their primary source of wealth (at least originally) from sectors that can be classified as 'rent-thick', that is, sectors in which there is significant connectivity with the state. Overall, 43 per cent of the total number of billionaires, accounting for 60 per cent of billionaire wealth in India, had their primary source of wealth from rent-thick sectors (see Gandhi and Walton 2012).

through its 'going global' policies of the 10th Five-Year Plan in the early 2000s.⁷ China embraced further globalisation by joining the World Trade Organization (WTO) in 2001. The prolonged negotiation process had provided motivation for reforms and its entry into the WTO benefited the country significantly through the exports channel. Outbound FDI got a boost as it complemented exports from China. Thus, for the past several years, a synthetic combination of exports and outbound FDI is at work through which Chinese firms are playing their part in the international economic arena and serving the foreign market.

Meanwhile, China and India have globalised at varying pace. The share in world trade increased marginally for India from 0.5 per cent in 1990 to 1.8 per cent in 2010. On the other hand, in the case of China, the same increased from 1.6 per cent in 1990 to 9.2 per cent in 2010 (see Kalirajan and Singh 2008; Panagariya and Sundaram 2013 for a comparative analysis of Indian and Chinese trade performance under trade liberalisation). Such differences can be observed using other measures of openness as well. Dimaranan et al. (2007) highlight the very sharp differences in the trade patterns of China and India: Within merchandise trade, both countries are dependent on manufactures, with China much more strongly integrated into production networks through trade in parts and components, radically different product mixture and services exports roughly twice as important for India as for China. In terms of share in global FDI inflows, China yet again does better than India. In 1990, India's share in global FDI inflows was 0.1 per cent and that of China was 1.7 per cent, which increased at a different pace in both the countries, with the result that the share stood at 2 per cent for India and 8.5 per cent for China in the year 2010 (The BRICS Report 2012: 43). Thus, China is deeply integrated into the wider global economy through the channels of trade and inward FDI. Inward FDI growth also helped China and India to augment technological capacity in the industrial sectors through collaborative efforts and spillover channels (Behera et al. 2012; Iyer 2009; Kathuria 2001; Liu 2008; Marin and Sasidharan 2010; Sasidharan and Kathuria 2011; Xu and Sheng 2012). It is to be noted that India's current account has always been in deficit,⁸ and is filled by foreign capital inflows primarily in the form of direct and portfolio investment. The surplus generated in the capital account has led to reserve accumulation and provided, with difficulty, the leeway for outward FDI.

The structure of the two economies is also different in many ways. Though agriculture was the backbone of the two economies prior to 1990, sectoral composition

⁷ The outward investment boom is considered to be a natural result of China's economic development and going-global strategy (Zhang 2009). The strategy encouraged outward investment through provision of information about foreign locations, the granting of incentives and gradual relaxation of foreign exchange controls.

⁸ Except during 2001–2 (US\$ 3,400 million), 2002–3 (US\$ 6,354 million) and 2003–4 (US\$ 14,083). The capital account has been in surplus, for example, US\$ 28,022 million in 2004–5, US\$ 7,395 million in 2008–9 and US\$ 67,756 million in 2011–12 (Source: Handbook of Statistics on Indian Economy, various issues, Reserve Bank of India).

has moved in different directions. For example, the share of the industry sector in the year 2000 was 20.7 per cent of GDP in India and 40.7 per cent in China. In the year 2009, the industry share was 28.2 per cent in India and 48.0 per cent in China. This shows that the industrial sector has emerged as a major contributor to the Chinese GDP in comparison to India.⁹ On the other hand, the services sector is more dominant in India than in China. In the year 2009, services contributed 54.6 per cent of GDP in India and 41.1 per cent in China (The BRICS Report 2012: 10).

China has achieved much higher economic growth than India in the last two decades. The differential growth is realised under different political environments—authoritarianism in China and democracy in India—and institutional set-ups. However, it has been claimed that authoritarianism is neither necessary nor sufficient for development, and that the relationship between democracy and development is actually much more complex than is allowed in standard discussion (Bardhan 2010).

Achievements on the economic front and globalisation have led to the growth of MNEs in both the countries, though under different ownership structures and institutional set-up, which is partly facilitated by government policies. These enterprises from China and India have shown aspiration to be regional and global players by engaging in outbound investments, driven by both economic and strategic considerations. The details of outbound investments—their features, motives and contributing factors—are discussed in the following two sections.

FEATURES OF OUTWARD INVESTMENTS BY CHINA AND INDIA

In the last decade, firms from China and India have invested in developed markets primarily through M&A.¹⁰ M&As are believed to be a less risky mode of entry into developed markets and an important means of accessing overseas assets urgently required for their global expansion (Hong 2011). On the other hand, greenfield investments are found to be more common in the case of investments in other developing and less developed countries, notwithstanding the data limitations in such cases.

SUCCESS RATE IN OVERSEAS ACQUISITION

Table 1 reports the recorded number of M&As and investment deals proposed by Chinese and Indian enterprises in the G-20 countries, the economically most dynamic group of countries, followed by the number of deals completed, and the completion

⁹ China has been consistently ranked the most competitive manufacturing nation in the world; see Global Manufacturing Competitiveness Index (2010, 2013) brought out by Deloitte and the US Council of Competitiveness.

¹⁰ Empirical evidence suggests that emerging market firms undertake acquisitions in developed countries in an incremental fashion (Rabbiosi et al. 2012).

Table 1
M&A and Investments by China and India in G-20 Countries
(Announcement date 2000–10)

<i>G-20 Countries</i>	<i>Number of Deals Proposed</i>		<i>Number of Deals Completed</i>		<i>Completion Rate (Percentage)</i>	
	<i>China</i>	<i>India</i>	<i>China</i>	<i>India</i>	<i>China</i>	<i>India</i>
Korea	13	1	8	0	61.54	0.00
Japan	28	3	19	2	67.86	66.67
UK	22	93	10	65	45.45	69.89
US	106	247	65	172	61.32	69.64
Canada	48	10	31	7	64.58	70.00
France	13	17	10	16	76.92	94.12
Germany	15	32	7	26	46.67	81.25
Italy	12	10	8	8	66.67	80.00
Argentina	3	4	2	3	66.67	75.00
Australia	96	27	46	14	47.92	51.85
Brazil	13	7	4	4	30.77	57.14
India	20	–	8	–	40.00	–
Mexico	3	4	2	2	66.67	50.00
Russia	12	3	5	3	41.67	100.00
Saudi Arabia	2	4	2	1	100.00	25.00
South Africa	5	25	1	14	20.00	56.00
Turkey	3	4	2	3	66.67	75.00
Indonesia	50	30	24	16	48.00	53.33
China	–	15	–	13	–	86.67
Total	464	536	254	369	54.74	68.84

Source: Author's compilation from Thomson Reuters Database.

percentage during 2000–10. It is observed that Chinese firms successfully completed 254 deals (out of 464 proposed deals) in the G-20 countries in the stated period. Out of the 254 deals completed, the highest number of investment deals were in the US (65) followed by Australia (46), Canada (31), Indonesia (24) and so on. On the other hand, Indian enterprises completed 369 deals (out of 536 proposed deals) in G-20 countries in the same period. The highest number of completed deals were in the US (172) followed by UK (65), Germany (26), France (16), Indonesia (16) and the like. Clearly, the US has been one of the important investment destinations for Indian MNEs. The primary aims of Indian MNEs to venture into the US and other developed markets were to access the latest technology, skills and knowledge that were either unavailable or of inadequate quality at home, to invest in research and development (R&D), and also to

commercialise the results of their creativity, especially in the pharmaceutical, chemical and information technology (IT) industries (Dasgupta 2010). It is to be noted that Indian enterprises proposed more deals than the Chinese and also completed a higher number of deals in the G-20 countries ~~than China~~ during 2000–10. The aggregate completion rate for India is 68.84 per cent as against 54.74 per cent for China.¹¹ The completion rate for India is better than China even at the individual country level, and particularly in top investment destination countries. This is primarily because of the fact that most of the outward investing Indian enterprises are in the private sector that are run on market principles, whereas most of the outward investing Chinese enterprises are state owned, where the corporate governance standards are weaker,¹² due to which they face scepticism and resistance from the target firms as well as the host country governments.¹³

Many of the mergers announced by Chinese enterprises ended in utter failure. However, in order to be successful globally, China reshaped its approach towards M&A. Instead of buying global brands, sales networks or goodwill, Chinese companies now mainly try to acquire concrete assets, such as mineral deposits, or state-of-the-art technologies and R&D facilities (Williamson and Raman 2011).

China has also undertaken economic cooperation-related investment in many countries in Asia, Latin America and Africa. In the context of Africa, there are suggestions that these investments are an expansion of China's influence to secure access to natural resources, among others (Brookes 2007). India too has renewed interest in Africa due to energy security concerns, although the country has a long way to go in the continent in terms of both trade and investment as compared to other countries (Paul 2014).

Not only has there been an increase in the number of investments from both China and India but they also involve large deals in terms of dollar value. Many multinational companies from China and India have successfully completed a considerable number of multibillion dollar deals. Over the years, such large deals have increased in number. For instance, there were a total of 14 M&A deals by MNEs from China (9) and India (5) worth over US\$ 1 billion and above in 2010.¹⁴

¹¹ Zhang et al. (2011) reported that the success rate of the acquisition deals (by China) with state-owned enterprise (SOE) targets is 41 per cent, significantly lower than others, such as 58 per cent for deals with private targets and 53 per cent for deals with listed company targets (which is close to ~~the~~ our figure of 54.74 per cent).

¹² See Yang et al. (2011) for a review of corporate governance in China, and Rajagopalan and Zhang (2008) for the evolution of and obstacles to corporate governance reforms in China and India.

¹³ Apart from SOEs, Chinese private enterprises have also been looked at with suspicion in some of the cases leading to blocking of investment deals by host governments (see *The Economist* 2012a). Furthermore, a report published on 8 October 2012 by the Intelligence Committee of America's House of Representatives calls for any attempt by Huawei and ZTE to buy American companies to be blocked by the government body that is responsible for reviewing foreign purchases of American assets on the grounds of security threat because of their opaque governance structure and links to China's communist party. However, the report is claimed to be devoid of hard evidence to support its draconian recommendations (see *The Economist* 2012b).

¹⁴ There were 152 M&A deals worth over US\$ 1 billion and above in 2010 by both developed and developing country MNEs, reported in World Investment Report 2011, UNCTAD.

The details of the M&A deals are reported in the Table A1 (Appendix), which contains information on the ultimate acquiring company, ultimate home economy, industry of the ultimate acquiring company, ultimate acquired company, ultimate host economy, industry of the ultimate acquired company, shares acquired, value of the deal and the rank of the deal in terms of value. Investments are in various sectors including energy and natural resources, telecommunications, motor vehicles, services, etc. Furthermore, a considerable amount of such investments are directed towards developed and resource-rich countries such as the United States, Canada, Brazil, Argentina and Australia. In terms of ownership of the acquiring company, the Indian enterprises in the list are private sector firms, whereas most of the Chinese companies are state-owned enterprises (SOEs). Similar observations can be made from the list of Chinese and Indian transnational corporations (TNCs) that appear in the top 100 non-financial TNCs from developing and transition economies (Table A2, Appendix). Nevertheless, Indian TNCs that appear in the list, by and large, score higher in terms of the transnationality index (TNI) in comparison to their Chinese counterparts, reflecting a higher level of global operations relative to their domestic activities.¹⁵

WHAT PROMPTED OUTBOUND INVESTMENTS?

MOTIVATIONS FOR OUTWARD INVESTMENTS

Evidence suggests that Chinese MNEs are motivated primarily by the quest for strategic resources and capabilities, and that the underlying rationale for such asset-seeking FDI is strategic needs. In an effort to enhance their competitive advantage in the global marketplace, Chinese firms use asset-seeking FDI to access and obtain strategic resources that are available in advanced foreign markets, but which are limited in their home country (Deng 2007, 2009). Chinese firms have also invested in advanced countries, particularly in the technology- and innovation-intensive sectors such as the electronics and computer segments, to access newly minted and internationally advanced technology. Securing assets and resources, such as raw materials and natural resources,¹⁶ fulfils not only the strategic need but also enhances global footprints, which is helpful in delivery of services in a wider market and acquiring managerial skills and brands abroad. By and large, both standard determinants and some China-specific factors are

¹⁵ Higher intensity of internationalisation of information technology (IT) firms from India has been observed by Paul and Gupta (2014).

¹⁶ Energy resources such as oil supply have been identified as a primary determinant of China's outward investment flow to African countries (Corkin 2007; Cheung et al. 2012; Wang 2012). However, China's capacity to transform the sub-Saharan region into a vibrant manufacturing base via FDI is still underdeveloped and quite limited (Ozawa and Bellak 2011).

found relevant in explaining outward direct investment of China (Cheung and Qian 2009; Cheung et al. 2012).

Market-related factors are found to have affected the location choices of Indian outward FDI (Milelli et al. 2010; Nunnenkamp et al. 2012). The Indian MNEs are primarily motivated by global ambitions of accessing worldwide marketing networks, brands and technology and also strategic assets in some cases (Kedron and Bagchi-Sen 2012; Pradhan 2010). The source of ownership advantage of Indian MNEs lies in their accumulation of skills for managing large multi-location operations across diverse cultures in India and their ability to deliver value for money with their frugal engineering skills honed up while catering to a large part of the income pyramid in India (Kumar 2008). It is worth noting that emerging country MNEs possess ownership advantages which could be different from the usual ones in developed country MNEs (see Ramamurti 2009, 2012). These ownership advantages of emerging MNEs could include their deep understanding of customer needs in emerging markets, the ability to function in difficult business environments, their ability to make products and services at ultra-low cost, etc. (Cuervo-Cazurra and Genc 2008; Govindarajan and Ramamurti 2011; Guillén and García-Canal 2009).

SECTORAL COMPOSITION

Most Chinese outbound investments are active in manufacturing sectors,¹⁷ although the industry profile is becoming increasingly diversified (Cernat and Parplies 2010). Indian outbound investments, on the other hand, are fairly diversified between manufacturing and services. Nevertheless, in recent times, the service sector has emerged as a major recipient of India's outward FDI (Das 2013; Mukherjee and Goyal 2013). Kumar and Chadha (2009) observed that Indian enterprises were undertaking outward FDI in manufacturing and services to pursue a strategy of horizontal expansion or internationalisation of operations seeking global footprints and local manufacturing bases across the borders. The outward FDI of Chinese enterprises, on the other hand, seem to be motivated by vertical integration seeking access to natural resources and raw materials and trading of finished goods produced in China.

CHARACTERISTICS OF OUTWARD INVESTING ENTERPRISES

Indian outward FDI is spearheaded by private sector-led (listed as well as non-listed) companies especially since the gradual liberalisation of capital account restrictions. The development of such enterprises was facilitated by restricting imports and foreign entry in the early period of their development before liberalisation of trade and

¹⁷ The significance of manufacturing industry on FDI towards North America and Europe could be the sign of strategic FDI in acquisition of advanced manufacturing technology (Miyamoto et al. 2011).

investment regimes in 1991 (Kumar 2008). On the other hand, the major chunk of Chinese outward investment is carried out by its SOEs.¹⁸ The dominance may continue given that the large SOEs are administered by the central government; such enterprises continue to enjoy certain privileges, especially in terms of government-supported finance, subsidies, procurement and regulations (Song et al. 2011).

The Chinese government also encourages private enterprises to invest abroad within the rationales of their own needs and policies. Meanwhile, domestic reforms in China have resulted in the falling share of state sector in the total economy (see Li and Putterman (2008) for a survey on the impact of reforms on China's SOEs). Since the 1990s, the private sector began to play a key role in competitive sectors, such as labour-intensive manufacturing industries, with SOEs concentrating on heavy industries, such as steel and machinery, the resource sectors, such as petroleum and minerals, and utilities and infrastructure, such as transport, electricity, water and telecommunications (Song et al. 2011). This type of concentration can also be seen in terms of outbound investments, with private enterprises investing abroad in order to utilise the market opportunities and SOEs pursuing strategic objectives that reflect Chinese long-term economic development priorities. However, the major constraint facing the private firms is the lack of access to financial resources, which affects their ability to invest abroad, compared to the SOEs that get favourable backing from state-owned banks vis-à-vis the private firms. This explains, to an extent, why outward investment from China is dominated by SOEs.

Prior to 2003, Chinese private firms were legally prohibited from investing abroad (Liang et al. 2012). Nevertheless, the policy change enabled private firms to invest globally.¹⁹ Internationalisation of Chinese private enterprises is also related to comparative advantages/disadvantages in resource endowment and organising capability relative to SOEs and foreign-invested enterprises. Organising capabilities of Chinese private enterprises are typically better than those of SOEs, but inferior to those of foreign-invested enterprises. Chinese private-owned enterprises tend to go international to exploit their advantages in organising capabilities compared with SOEs, and to upgrade their organising capabilities compared with foreign-invested enterprises (Liang et al. 2012).

¹⁸ As per data reported by UNCTAD, outward FDI by Chinese state-owned TNCs was US\$ 38,899 million in 2010. On the other hand, outward FDI by Indian state-owned TNCs was US\$ 487 million in the same year. The total outward FDI by state-owned TNCs from developing countries was reported at US\$ 85,698 million in 2010.

¹⁹ To help Chinese firms invest abroad, the Chinese central government had signed bilateral investment treaties with 103 countries and double taxation treaties with 68 countries by early 2003 (Wu 2005). As of 1 June 2012, China concluded bilateral investment agreements with 128 countries. In contrast, as of 1 June 2012, India had concluded bilateral investment agreements with only 83 countries. China and India had also concluded double taxation agreements with 107 and 80 countries, respectively, as of 1 June 2011 (as per data reported in Division of Investment and Enterprise, UNCTAD). The terms specified in bilateral investment treaties provide required guidance in solving ~~any~~ dispute involving inward or outward FDI.

Chinese private enterprises are also expected to increase their outward investment in the near future. However, Chinese private firms may not be able to match the SOEs (or their Indian counterparts) in terms of the level of investment abroad. Though ~~there is~~ a burgeoning private capitalism ~~that~~ is developing in China, the state still controls the key sectors directly or indirectly.

GOVERNMENT POLICY TOWARDS OUTWARD INVESTMENTS

The Chinese government's policy towards outbound investments is characterised by active promotion through financial and fiscal incentives to firms, which is an integral part of China's economic development strategy, though it was restrictive in nature in the early stage of economic reforms. Earlier, Chinese coastal-oriented export-led development strategy opened up 14 coastal cities in 1988 and four special economic zones. Large Chinese SOEs were for the first time authorised to invest overseas and this was linked with the government's political and economic agenda of expanding China's trade (Kumar and Chadha 2009). On the other hand, the role of the government in promoting outward FDI in India is a passive one, which is limited to providing policy signals and reforms. The increase in outward FDI from India is due to a favourable policy regime subsequent to the introduction of the Foreign Exchange Management Act (FEMA) in June 2000.²⁰ In particular, Indian firms were permitted to invest abroad up to 100 per cent of their net worth in 2003–4. The limit was subsequently revised, to meet the growing needs of Indian firms, to 200 per cent of net worth in 2005–6, to 300 per cent of net worth in 2007–8 and to 400 per cent of net worth in 2007–8 (Khan 2012; RBI 2010). Improved macroeconomic performance, along with the growth of Indian corporates, has helped India navigate to a more open capital account and outward FDI policy regime over time, thereby facilitating the private enterprises to invest abroad.

FINANCING OF INVESTMENTS

Indian firms have a variety of options for financing of overseas investments. These options include purchasing of foreign exchange onshore from an authorised dealer in India, capitalisation of foreign currency proceeds to be received from the foreign entity on account of exports, fees, royalties or any other dues from the foreign entity for

²⁰ In 1995, the task relating to approvals for overseas investment was transferred from the Ministry of Commerce to the RBI to provide a single-window clearance mechanism. See Athukorala (2009), Gopinath (2007), Khan (2012), Pradhan (2008) and RBI (2010) for policy trends and a chronology of major reforms in India's outward FDI; see Sauvart and Chen (2014) for a review of China's regulatory framework for outward FDI.

supply of technical know-how, consultancy, managerial and other services, swapping of shares of the Indian entity with those of the overseas entity, use of balances held in Exchange Earners' Foreign Currency (EEFC) accounts of the Indian entity maintained with an authorised dealer, foreign currency proceeds through external commercial borrowings (ECBs)/foreign currency convertible bonds (FCCBs) and exchange of American depositary receipts (ADRs)/global depositary receipts (GDRs) issued in accordance with the scheme for issue of FCCBs (see Khan 2012). Indian firms are also benefiting from the emerging global FDI environment which is conducive for M&A.²¹ Stock financing is also viewed as a possible remedy for reducing information asymmetry and lowering corporate-governance-related risk in cross-border M&As (Dutta et al. 2013). The rapid growth of FDI outflows and the spurt in foreign acquisitions by Indian firms, in part, are attributed to the conjectural factors implicit in the liberalisation of the policy regime and the greater access to the financial market (Nayyar 2008).

Accumulation of massive foreign exchange reserves through trade surplus has allowed Chinese authorities to encourage outward investment to utilise the surplus. Outward-investing Chinese firms can have access to capital at a lower cost from the state or the Chinese state-owned banks. Furthermore, China's Export-Import Bank also provides loans to firms for outward investments. Fiscal incentives are also provided to firms that use Chinese machinery, plant and equipment in their overseas ventures (Kumar and Chadha 2009: 251). Sovereign wealth funds (SWFs) are another source of capital for outward FDI. SWFs have contributed to the outward FDI of China, with the establishment of the China Investment Corporation (CIC) in 2007 (Athreye and Kapur 2009).²² India, on the other hand, has only considered but not established any SWF. The country has not reached a stage where it can commit foreign exchange reserves to a SWF as its own requirements could change quickly due to a sudden outflow of portfolio investments. The acquisitions of strategic assets by Chinese SWFs (and national oil companies), such as of oil and gas, are both aimed at contributing to energy security and commercially driven (Jiang and Sinton 2011; Wu and Seah 2008; Wu et al. 2011). Nevertheless, the distinction between commercial and non-commercial objectives of SWFs is not always clear-cut (Park and Estrada 2009). It may be noted that overseas financing (issue of stocks on overseas capital market or selling of bonds on overseas capital market) continues to be a less attractive source of finance for Chinese firms (China Goes Global 2010). In recent times, private capital has also helped Chinese firms to venture abroad (see *The Economist* 2012c).

²¹ Many Indian firms also resort to leverage buyout option.

²² For a discussion on the birth of CIC, its portfolio allocation and investment strategy, impact and challenges, see Wu and Seah (2008); for the CIC's post-crisis investment strategy, see Wu et al. (2011); and for challenges of developing Asia's SWF's to undertake FDI on a significant scale, see Park and Estrada (2009) and Ramamurti (2011).

GOING FORWARD

Economic progress, as well as outward FDI, in China and India, has been guided by the chosen development paradigm within the political and economic ideology of the two countries. Outbound investments from China and India differ in terms of the institutional environment, motivation, sectoral composition, etc. The main differences with regard to outward investment by Indian and Chinese enterprises arise in the degree of involvement of the public sector enterprises, financing of investments, success rate of proposed M&As, sectoral composition, investment motives, etc., despite encouraging government policy in both the countries.

There is not much overlap in the outbound FDI experience of the two countries (Sun et al. 2012). Nevertheless, potential competition between the two countries cannot be ruled out especially in the case of regional investments in Asia. Competition between China and India can be observed, for instance, in the energy sector (Katakey and Duce 2010; Modi 2013; Sinha and Dadwal 2005). There is potential for both countries to learn from each other, for example, managing cross-border alliances and economic diplomacy (Hong 2011). The outbound FDI experience of the two countries could also guide other emerging countries in shaping their outward FDI policies.

IMPLICATION FOR REFORMS

It is claimed that outward direct investment by Chinese firms was not concentrated in industries that performed well either in exporting or domestically (Huang and Wang 2011). Instead, investments are made in countries where they could either learn advanced technologies or secure stable commodity supplies thereby strengthening industries at home²³ through the acquisition of management skills, advanced technology, brands or raw material supply. Domestic regulatory and financial sector reforms in China that treat all types of ownership firms equally will not only encourage competition and efficiency in the economy but also help the growth of private MNEs and provide equal opportunity to such enterprises to invest abroad, especially since more difficulties are faced in host countries by SOEs while investing abroad due to the strategic motive, which is a concern of the target country governments.

In the Indian case too, there is a need for further reform to improve the ease of doing business at home so that outward FDI does not arise due to domestic constraints.

²³ It is also argued that the motivation of acquiring strategic assets useful for reinforcing a competitive position in the domestic market seems to be only part of a transition phase of Chinese MNEs' international development as these MNEs could also aim at reaching a position of global leadership (Parmentola 2011).

Private investors still require a large number of permissions from the government to start a business. The existence of myriad regulations at the state level raises the cost of entry and operation of business in India.

It may be noted that the recent launch of the *Make in India* programme in September 2014 is expected to improve the business environment at home, attract FDI across sectors and create millions of jobs, provided reforms are carried out across several dimensions including taxation, land and labour laws. The programme includes new initiatives designed to facilitate investment, foster innovation, protect intellectual property and build world-class manufacturing infrastructure. This could also make investment at home by domestic firms more attractive vis-à-vis outward FDI. As a result, divergence might arise in the outward FDI trajectory of India in comparison to China, as the latter is expected to continue on the track of outward FDI.

CHALLENGES AND IMPACT

There are various challenges facing both countries that must be addressed in order to be successful in investing abroad so that direct or indirect benefits of such investment outweigh the cost, which can also stand as an example to other developing countries.²⁴ Such outward FDI also needs to be maintained in a sustainable way so that it does not come at the expense of domestic investments. Thus, challenges are manifold, ranging from macroeconomic, financial and institutional to governance related. Macroeconomic challenges include maintaining comfortable levels of foreign exchange reserves, stable exchange rate, encouraging financial sector development and deepening for lower cost of capital, regulating leverage buyout and excessive external commercial borrowings, ~~etc.~~ so that pressure on international reserves can be minimised. Institutional and governance issues at home are also to be addressed so that outflow does not happen due to domestic compulsions, such as, corruption, difficulty of doing business, infrastructural constraints and so on.²⁵ Further reforms in all these areas in both the countries would be beneficial for both domestic and international investments. Finally, firm-level challenges with respect to corporate governance,²⁶ legal obstacles and managing across diverse cultures have also to be dealt

²⁴Through outward FDI into any sectors, industries or regions, there should be intra-industry productivity spillovers from foreign firms to domestic firms within the same industry, mainly through reduction in production cost, technology transfer and R&D spillovers (Lian and Ma 2011).

²⁵The arrival of Chinese and Indian firms in Europe is linked to home country constraints (see Milelli et al. 2010).

²⁶Globerman and Shapiro (2009) argue that voluntary initiatives on the part of Chinese MNCs to improve corporate governance practices and meet transparency standards recommended by international organisations, such as the World Bank, should be seen as investments in maintaining secure access to (the US) domestic market for both exports and capital investments.

with. In particular, the success of Chinese MNEs will depend on bridging the cultural gap between Eastern and Western companies and successful integration of Eastern management philosophy with Western practices (Nguyen et al. 2010). In the light of the concerns and challenges facing outward investments from China and India, both national and international investment promotion agencies can play a vital role in mitigating the legitimate concerns and challenges. Nevertheless, outward investment from China and India is expected to benefit both home and the host countries in multiple ways including employment creation, technology transfer, R&D, etc. Empirical evidence on this front is encouraging (Buckley et al. 2011; Milelli et al. 2010; Tiwari and Herstatt 2010; Whalley and Weisbrod 2012).²⁷ The outbound FDI experience of China and India could guide other developing countries in shaping their outward FDI trajectories.

In conclusion, the comparison and contrast of outward FDI by Chinese and Indian MNEs reveal that there are more differences than similarities in the investment development trajectory of the two countries. Major differences are observed with respect to the financing of investment, success in overseas M&As, degree of involvement of public sector enterprises, sectoral composition, investment motives, challenges in the process of outward FDI and so on. The article essentially provides an overall perspective of the outward FDI trajectory of China and India, as it is based on empirical assessment of various parameters and complemented by evidence from the literature. It also provides insights for managing the phenomenon of outward FDI from China and India, in particular, and argues for economic and institutional reforms, ~~as~~ specifically highlighted above, in the light of the challenges faced by MNEs from the two countries in the process of outward FDI.

²⁷ Tiwari and Herstatt (2010), analysing Indian investment in Germany, found evidence of positive net job balance in the host country, and active transfer of technology between home and host country in most cases. Milelli et al. (2010) observed that Chinese firms created extra jobs in Europe. Buckley et al. (2011) investigated the impact of the entry of emerging MNEs from Brazil, Russia, India and China on the performance of firms acquired in Europe, North America and Japan between 2000 and 2007. The study found that emerging MNEs contribute to increasing the target firms' productivity and sales and to slowing down their loss of jobs, although they do not always acquire firms with a high pre-acquisition performance and do not significantly increase the post-acquisition profitability of the target firms. Whalley and Weisbrod (2012) observed that a significant portion of the growth in Sub-Saharan Africa in the 3 years before the global financial crisis and also in the 2 years afterwards can be attributed to Chinese investment.

APPENDIX

Table A1
Cross-Border M&A Deals by China and India Worth Over US\$1 Billion Completed in 2010

<i>Ultimate Acquiring Company</i>	<i>Ultimate Home Economy</i>	<i>Industry of the Ultimate Acquiring Company</i>	<i>Ultimate Company</i>	<i>Ultimate Host Economy</i>	<i>Industry of the Ultimate Acquired Company</i>	<i>Shares Acquired</i>	<i>Value (\$ billion)</i>	<i>Rank</i>
Bharti Airtel Ltd.	India	Telephone communications, except radio-telephone	Zain Group	Kuwait	Radio-telephone communications	100	10.7	2
Sinopec Group	China	Crude petroleum and natural gas	Repsol YPF SA	Spain	Petroleum refining	40	7.1	10
Investor Group	India	Investors, nec	Republic of Venezuela-Carabobo	Venezuela	Crude petroleum and natural gas	40	4.8	16
GAIG	China	Motor vehicles and passenger car bodies	Denway Motors Ltd.	Hong Kong, China	Motor vehicle parts and accessories	62	4.1	21
China National Offshore Oil Corporation	China	Crude petroleum and natural gas	Bridas Energy Holdings Ltd.	Argentina	Offices of holding companies, nec	50	3.1	40
Adani Enterprises Ltd.	India	Business services, nec	Linc Energy Ltd.	Australia	Coal mining services	100	2.7	45
CNPC	China	Crude petroleum and natural gas	Athabasca Oil Sands Corp	Canada	Crude petroleum and natural gas	60	1.7	79
GTL Infrastructure Ltd.	India	Radio-telephone communications	Usaha Tegas Sdn Bhd	Malaysia	Investors, nec	100	1.7	82
State Grid Corporation of China	China	Electric services	Expansion Transmissao Itumbiara	Brazil	Power, distribution and specialty transformers	75	1.7	83
Peoples Republic of China	China	National government	AES Corp	United States	Electric services	16	1.6	91

(Table A1 Continued)

(Table A1 Continued)

<i>Ultimate Acquiring Company</i>	<i>Ultimate Home Economy</i>	<i>Industry of the Ultimate Acquiring Company</i>	<i>Ultimate Acquired Company</i>	<i>Ultimate Host Economy</i>	<i>Industry of the Ultimate Acquired Company</i>	<i>Shares Acquired</i>	<i>Value (\$ billion)</i>	<i>Rank</i>
Zhejiang Geely Holding Group Co Ltd.	China	Motor vehicles and passenger car bodies	Volvo AB	Sweden	Motor vehicles and passenger car bodies	100	1.5	99
Tianjin Municipal Tanggu	China	City agency	Tianjin Port(Group) Co Ltd.	China	Marine cargo handling	57	1.5	102
Reliance Industries Ltd.	India	Crude petroleum and natural gas	Pioneer Natural Resources Co	United States	Crude petroleum and natural gas	38	1.1	134
China National Offshore Oil Corporation	China	Crude petroleum and natural gas	Chesapeake Energy Corporation	United States	Crude petroleum and natural gas	33	1.1	140

Source: Authors' compilation from UNCTAD.

Table A2
TNCs from China and India in the List of Top 100 Non-financial TNCs from Developing and Transition Economies, 2009
(Ranked by Foreign Assets, Millions of Dollars and Number of Employees)

Rank	Corporation	Home Country	Industry	Assets		Sales		Employment		TNI*
				Foreign	Total	Foreign	Total	Foreign	Total	
2	CITIC Group	China	Diversified	43 814	315 433	10 878	30 605	25 285	125 215	23.2
7	China Ocean Shipping (Group) Company	China	Transport and storage	28 092	36 287	18 354	27 908	4 207	71 584	49.7
14	Tata Steel Ltd.	India	Metal and metal products	15 606	24 419	15 921	21 580	47 168	81 269	65.2
23	China National Petroleum Corporation	China	Petroleum expl./ref./distr.	11 594	325 327	4 732	178 343	29 877	1 585 000	2.7
25	Tata Motors Ltd.	India	Automobile	11 297	20 231	11 495	19 521	17 728	49 856	50.1
30	Oil and Natural Gas Corporation Ltd.	India	Petroleum expl./ref./distr.	10 447	37 223	2 912	21 445	3 896	32 826	17.8
33	Hindalco Industries Ltd.	India	Diversified	9,372	15 406	9,739	12 764	11 886	19 539	66.0
41	Sinochem Group	China	Petroleum expl./ref./distr.	8 124	25 132	27 492	35 577	225	42 282	36.7
47	China National Offshore Oil Corporation	China	Petroleum expl./ref./distr.	6,648	75 913	4,898	30 680	1,739	51 000	9.4
67	Suzlon Energy Ltd.	India	Diversified	4,648	6 499	3,481	4 346	9,298	13 000	74.4
69	Tata Consultancy Services	India	Other services	4,360	6 109	5,739	6 329	10 400	160 429	56.2
72	Reliance Communications Ltd.	India	Telecommunications	4,256	20 766	1,006	4 664	6,348	30 974	20.9
73	Lenovo Group Ltd.	China	Electrical and electronic equipment	3,957	8 956	8,713	16 605	5,130	22 205	39.9
77	China Railway Construction Corporation Ltd.	China	Construction	3,580	41 444	3,265	50 501	20 426	209 103	8.3
84	ZTE Corporation	China	Other consumer goods	3,017	10 173	4,372	8 823	21 821	70 345	36.7
93	China Minmetals Corporation	China	Metal and metal products	2,352	18 889	3,994	24 956	12 535	100 656	13.6

Source: Author's compilation from UNCTAD.

Note: *TNI, the transnationality index, is the average of the three ratios, that is, foreign assets to total assets, foreign sales to total sales and foreign employment to total employment.

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