

Functioning of FDI Companies in India: Expectations and Experiences

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with Emphasis on the Manufacturing Sector**

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**India's Post-1991 Inward FDI Experience:
Looking Beyond the Aggregates**

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Introduction

The issue of earning in foreign currencies by foreign companies for resource-constrained developing countries has been a matter of interest for a long time. It has usually been assumed that in their host economies, foreign companies are more likely to register larger foreign exchange earnings than their domestic counterparts due to their advantages of owning superior technologies and established brand names, as also easier access to global markets. However, the reality conveys a sharply contrasting picture. A number of studies covering different periods in the pre-liberalisation period for India showed that both trade balance and net foreign exchange earnings on their account were negative.¹ There has also been serious discussion on the long term impact of FDI on domestic savings and investment for the developing countries.²

The economic reforms that the government of India undertook in 1991 highlighted the advantages that could accrue from greater involvement of FDI in the manufacturing sector. The Statement on Industrial Policy stated, “[F]oreign investment and technology collaboration will be welcomed to obtain higher technology, to increase exports and to expand the production base”.³ The Statement also placed emphasis on building the country’s “ability to pay for imports through our own foreign exchange earnings”. In keeping with its pronouncements, the Government of India decided to remove the policy bottlenecks which were perceived to have prevented the economy to benefit from foreign companies’ capabilities. This approach was also advocated by highly reputed international scholars. One such view was the following:

The question of direct foreign investment (DFI) is related to the question of trade and industrial policy, reforms in one suggesting and even requiring reforms in the other.

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¹ See for instance, S. K. Goyal, *Impact of Foreign Subsidiaries on India’s Balance of Payments*, a report submitted to the UNCTC Bangkok Unit, 1979. K.S. Chalapati Rao, "An Evaluation of Export Policies and the Export Performance of Large Private Companies", in Pitou van Dijck and K.S. Chalapati Rao, *India's Trade Policy and Export Performance of Industry*, 1994, Sage, New Delhi.

² Biswajit Dhar and Saikat Sinha Roy, "Foreign Direct Investment and Domestic Savings-Investment Behaviour: Developing Countries Experience", *Economic and Political Weekly*, Vol - XXXI No. 35-36-37, September 14, 1996, pp. 2547-52.

³ Statement on Industrial Policy, July 24, 1991.

... inward oriented trade policies lead to DFI which is aimed at the domestic market where as outward oriented trade policies encourage DFI which seeks global markets.

... “export performance requirements” which have contributed to the relative unattractiveness of India as a host country for DFI can be eliminated now that we are turning rapidly to an outward oriented set of trade and industrial policies.⁴

The authors also emphasised that

...a compromise in regard to the acceptance of intellectual property rules (however “unfair”), as demanded by the United States and in fact by other OECD countries, should be treated simply as a (minor) cost of attracting DFI. For, multinationals now treat the acceptance of such rules as an index of the seriousness of a country in attracting DFI.⁵

Following the change in the orientation of policies vis-à-vis FDI, 100 percent foreign ownership was gradually allowed in all the manufacturing sectors⁶, mainly through the automatic route. As was noted earlier, the Government of India did not impose any conditions on the foreign investors, like transfer of technology, while it went about dismantling the regulations existing earlier in order to facilitate entry of FDI - it expected that the benefits from FDI would accrue automatically. It also expected that liberal payment terms would encourage transfer of technology. (See Box-A) In fact, in the early days of opening up, foreign investors were enticed with the prospect of serving domestic market having a large middle class population with high purchasing power.⁷ It is, however, now well recognised that the domestic market has been the main focus of FDI companies. Even the recent empirical evidence underlines that foreign affiliated manufacturing companies are net spenders of foreign exchange whether seen on the trade front or in association with other items.⁸

Balances in Foreign Exchange Transactions

While there could be the issue of representative character of studies based on the widely used corporate databases like the *Prowess* and the *Capitaline*, it is important to note that even Foreign Affiliates Trade Statistics collected by the Reserve Bank of India along with the Census of Foreign Liabilities and Assets of Foreign Direct Investment Companies (FLA-FDI Census) underlines the negative trade balances on account of foreign subsidiaries in the manufacturing sector. These

⁴ See: Jagdish Bhagwati and T.N. Srinivasan, *India's Economic Reforms*, July 1993, p.44.

⁵ *Ibid.*, p. iv.

⁶ Tobacco products and defence industries were the two exceptions for a number of years. Now there has been a gradual opening up of the defence industries also)

⁷ For instance, the then Prime Minister said at the World Economic Forum' meet in Davos on February 3, 1992 that “India is a huge market. If you go down to the people it is mind boggling”. See: “Rao invites foreign investment: Further Nationalization Ruled Out”, in *The Statesman*, February 4, 1992. Accessed from ISID Newspaper Clippings Archives, *Transnational Corporations*, Volume I, January-May 1992, page 53A.

⁸ Swati Verma, “Current Account Fallout of FDI in Post-Reform India: Evidence from Manufacturing Sector”, *Economic and Political Weekly*, Vol. L No. 39, September 26, 2015, pp. 45-53.

Surveys, which cover the largest number of foreign subsidiaries, reveal that in 2013-14 in most branches of manufacturing the subsidiaries ran deficits on the trade account. (Table-1) However, the subsidiaries of foreign companies operating in India had together generated surplus on the trade account, which was possible only because of contribution made by the companies in Information and Communication sector. The manufacturing companies also exhibited very high degree of import dependence, raising further concern about the weak backward linkages. The previous Survey for the year 2012-13 and the just released Survey for the year 2014-15 also presented similar results.

Box-A: Timeline of Policy and Procedural Changes Relating to Technology Payments	
1991	<ul style="list-style-type: none"> • The Statement on Industrial Policy categorically mentioned that “[F]oreign equity proposals need not necessarily be accompanied by foreign technology agreements”. • Automatic approval will be given for foreign technology agreements in high priority industries up to a lump sum payment of Rs 1 crore, 5% royalty for domestic sales and 8% for exports, subject to total payment of 8% of sales over a 10 year period from date of agreement or 7 years from commencement of production.
1996	<ul style="list-style-type: none"> • The existing ceiling of Rs 1 crore by way of payment of lump sum fee for automatic approval for foreign collaboration raised to US \$ 2 million.
1998	<ul style="list-style-type: none"> • Automatic route for FDI and/or technology collaboration was withdrawn for those who have or had any previous joint venture or technology transfer/trade mark agreement in the same or allied field in India. Henceforth government approval would be required in such cases.
2000	<ul style="list-style-type: none"> • The condition of Automatic route for FDI and/or technology collaboration for those who have or had any previous joint venture or technology transfer/trade mark agreement in the same or allied field in India was removed for IT sector. • Payment of royalty up to 8% for export and 5% for domestic sales by wholly owned subsidiaries to parent companies is allowed under automatic route without any durational restriction for royalty payments. • Payment of royalty up to 2% for export and 1% for domestic sales is allowed under automatic route on use of trademarks and brand names for the foreign collaborator without technology transfer.
2001	<ul style="list-style-type: none"> • Multilateral institutions were freed from the restrictions applicable to those who have or had any previous joint venture or technology transfer/trade mark agreement in the same or allied field in India.
2003	<ul style="list-style-type: none"> • The durational restriction for payment of royalty for technology transfer and brand name use for other companies was also removed.
2009	<ul style="list-style-type: none"> • Payment of royalty, lump sum fee for transfer of technology and payment for use of trademark/brand name under automatic route was permitted.

Table-1: Sector-wise Exports, Imports, Trade Balance of 9,081 Foreign Subsidiaries during 2013-14
(Amount in Rs billion)

Activity	No. of Cos	Exports	Imports	Trade Balance	Share of Imports to Purchases (%)
(1)	(2)	(3)	(4)	(5)	(6)
A. Agriculture-related, Plantations & Allied activities	25	5.5	4.2	1.3	11.1
B. Mining	36	7.8	9.9	-2.1	12.7
C. Manufacturing	2,166	2,284.1	3,498.2	-1,214.1	50.7
- Computer, electronic and optical products	56	165.9	536.9	-371.0	78.6
- Coke and refined petroleum products	9	414.5	740.1	-325.6	81.5
- Food products	92	371.9	668.6	-296.7	68.2
- Chemicals and chemical products	160	117.5	172.9	-55.4	46.3
- Electrical equipment	132	97.0	151.8	-54.8	36.4
- Rubber and plastics products	77	21.5	38.2	-16.7	48.7
- Manufacture of paper and paper products	19	7.1	22.9	-15.8	58.4
- Basic metals	25	43.5	56.2	-12.7	19.0
- Fabricated metal products, except machinery & equipment	79	8.4	15.7	-7.3	38.1
- Motor vehicles, trailers and semi-trailers	75	390.1	385.5	4.6	26.3
- Wearing Apparel	20	9.9	3.4	6.5	34.7
- Textiles	30	16.7	8.7	8.0	40.7
- Pharmaceuticals, medicinal & chemical products	100	108.5	80.4	28.1	45.7
- Machinery and equipment n.e.c.	355	156.1	119.2	36.9	35.6
- Other manufacturing	937	355.5	497.7	-142.2	46.4
D. Electricity, gas, steam and air conditioning supply	72	1.5	5.2	-3.7	25.0
E. Water supply; sewerage, waste mgmt and remediation activities	31	0.3	0.6	-0.3	12.5
F. Construction	187	20.5	31.1	-10.6	22.4
G. Services	4,968	2,580.4	846.7	1,733.7	35.1
- Information and communication	1,920	2007.7	202.2	1805.5	25.4
- Financial and insurance activities	243	67.0	6.3	60.7	6.9
- Transportation and storage	163	63.6	25.3	38.3	25.1
- Wholesale and retail trade; repair of motor vehicles	783	153.4	548.2	-394.8	51.3
- Other Services activities	1,859	288.7	64.7	224.0	18.1
Total	*7,485	4,900.1	4,395.9	504.2	45.8
<i>Memorandum Items</i>					
<i>Manufacturing 2012-13</i>		1,539.6	2,642.7	-1,103.1	58.3
<i>2013-14</i>		2,284.1	3,498.2	-1,214.1	50.7
<i>2014-15</i>		2,505.7	3,474.0	-968.3	49.7
<i>Services 2012-13</i>		1,936.1	625.3	1,310.8	32.3
<i>2013-14</i>		2,580.4	846.7	1,733.7	35.1
<i>2014-15</i>		3,093.9	1,163.2	1,930.7	36.9
<i>Total 2012-13</i>		3,509.5	3,316.0	193.5	44.1
<i>2013-14</i>		4,900.1	4,395.9	504.2	45.8
<i>2014-15</i>		5,637.4	4,695.2	942.2	44.9

Source: Based on the data released by the Reserve Bank of India.

(https://rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=33035)

* Out of the 9,081 subsidiaries 7,485 reported sales, 5,554 reported exports.

For the year 2014-15, of the 10,777 subsidiary companies, 8,032 reported sales, 5,400 companies reported purchases and 6,024 reported exports and 4,033 reported imports.

Note: (i) One is not sure whether the tabulations are for only those companies which reported sales. (ii) RBI does not explain the items covered under purchases.

However, the aggregative numbers provided by the RBI need to be explained for a better understanding of the performance of foreign subsidiaries. First, the aggregative numbers make no distinction between older and newer companies. But newer companies may not start exporting soon after setting up business in India, while there could be import of capital goods and some traded items to start the operations, which, in part, could be because these companies may not be able to immediately identify local suppliers of raw materials and components. These factors could reflect on the adverse trade balance and greater import dependence. Further, RBI has pointed out that of the 9,081 subsidiaries included in the 2013-14 Survey, sales data was reported by 7,485 companies. By implication those companies which reported data on exports should be among the 7,485 only. It is possible that the RBI has reported imports and purchases data for 9,081 companies and sales and exports data for 7,485 companies.

On the other hand, one does not find any explanation from the RBI as to what the data on purchases, the denominator for calculating the imports to purchases ratio represent. We presume that they include all purchases -- both goods and services. If that is the case, the comparison of imports with such purchases would not be appropriate especially because imports are limited to capital goods, raw materials, components and spares as also finished goods. If imports include payments for services then the ratio would not reveal the actual position with regard to trade in goods, a concept more relevant for manufacturing companies. The questionnaire merely asks for information on (i) Domestic Sales, (ii) Exports, (iii) Domestic Purchases and (iv) Imports. If this is the case, the appropriate ratios would turn out to be even more adverse. This appears to be the case from a reading of *Manual on Statistics of International Trade in Services 2010*.⁹ There could also be classification issues as to what extent a company could be treated as a manufacturing one if it is also trading in same or similar items. The traded items would increase the ratio and do not reveal the extent of indigenisation of actual manufacturing. For instance, while one can understand the high imports to sales ratio of 81.5% in case of coke & refined petroleum products, the fact that it is only marginally lower at 78.6% for the 'computer, electronic & optical products' category is something that needs a closer look. Was it due to heavy dependence on imported materials or because of substantial quantities of finished goods imports? On the other hand, 'Pharmaceuticals, medicinal and chemical products' being a net earner on trade account may not reflect the high original export propensity of foreign subsidiaries if seen in the context of a few major exporting Indian pharmaceutical companies being taken over and the older MNC pharmaceutical companies' tendency to serve the domestic market more. Even the food products group is among the top losers. Interestingly, the trading companies too ran deficits.

⁹ [http://unstats.un.org/unsd/tradeserv/TFSITS/msits2010/docs/MSITS%202010%20M86%20\(E\)%20web.pdf](http://unstats.un.org/unsd/tradeserv/TFSITS/msits2010/docs/MSITS%202010%20M86%20(E)%20web.pdf)

Since the foreign exchange earnings would consist of earnings from export of services also, if some of the manufacturing companies' earnings consist of services exports, the contribution of foreign subsidiaries to manufacturing exports could be an overestimate. Disaggregated tabulations coupled with explanation on the concepts used could have helped in a better understanding of the contribution of foreign subsidiaries in the manufacturing sector.

Growing Importance of Non-trade Transactions

The developments during the recent past also suggest that expenditure in foreign currencies other than in the form of imports has become important both relative to imports and in absolute terms.¹⁰ While our reservation about the suitability of 10% cut-off for identifying an FDI company remains, RBI's studies on 'Finances of Foreign Direct Investment Companies', based on this definition, show that the share of imports in total foreign exchange expenditure fell from 84.9% in 1992-93 to 80.9 in 2004-05 and further to 77.2% in 2012-13. Correspondingly, however, the share of dividends in total expenditure remained almost stable, though with some slight fluctuations in between: 3.9% in 1992-93 and 3.6% in 2004-05. The corresponding figure for 2012-13 is not available. It should be noted that these figures do get affected by the changing number of companies in different years. While dividend payments -- whether high or low -- have not attracted public attention, the burgeoning royalty payments was discussed at length, because the focus was on the listed companies, as it was seen to be a way of denying the non-controlling shareholders of FDI companies their due.

Linked to this was the possibility that royalty payments may not be directly related to technology transfer as they could also be used as substitutes for dividend payments. While earning net foreign exchange is important by itself, the high royalty payments take the issue much further. The fact of transfer pricing and other practices by MNCs to save taxes is quite real and even developed economies are seized of this matter.¹¹ While dividends can be paid out of the profits earned, the additional advantage of royalty and other payments for FDI companies is that they reduce tax liability on one hand and on the other, there is no need to earn/declare profits which is generally a pre-requisite in case of dividend payments. Further, unlike import and export of goods, payments for technology and services rendered/received, etc. are more ambiguous in their determination and there could be higher propensity to transfer profits out of host developing countries or park surpluses in tax havens.

¹⁰ Swati Verma, *op. cit.*

¹¹ This has been the focus of OECD/G20 Base Erosion and Profit Shifting project. The developing countries are interested in getting the details of interest payments, royalty payments and "especially related party service fees". See: OECD/G20 Base Erosion and Profit Shifting Project, 2015 Final Reports, Executive Summaries, accessed at <http://www.oecd.org/ctp/beps-reports-2015-executive-summaries.pdf>

Gleanings from RBI's Finances of FDI Companies Studies

RBI studies on 'Finances of Foreign Direct Investment Companies' show that at the aggregate level FDI companies in the manufacturing sector consistently paid at higher rates of royalty than non-FDI companies over the five year period 2007-08 to 2011-12. Interestingly, the latest study in the series does not cover this aspect. The difference between the two types of companies was not so stark in case of services. Royalty rates were far higher for manufacturing FDI companies compared to those in the services sector. Interestingly, among the FDI companies, the ratio of royalty to sales increased progressively with foreign share and it was the highest for companies with foreign shares of 50% and more. (Table-2) Within the manufacturing sector, FDI companies paid at far higher rates in case of the transport equipments sector. In case of chemicals and chemical products and electrical machinery and apparatus sectors the rates are higher but considerably lower than those for the transport equipment sector. (Table-3) Also, RBI data consistently show that non-FDI companies at the aggregate level as also in the manufacturing sector have much higher export propensity compared to FDI companies. Leaving aside 2007-08, better export performance of non-FDI companies was evident in case of services sector also. No consistent pattern could, however, be discerned when the FDI companies' data was analysed according to the extent of foreign share suggesting that higher foreign shares are not necessarily associated with better export orientation. (Table-4)

Table-2: Rates of Royalty paid by FDI and Non-FDI Companies

Year	Classification	Royalty Payment to Sales Ratio (%)				
		2007-08	2008-09	2009-10	2010-11	2011-12
All Companies	FDI	0.46	0.51	0.68	0.75	0.59
	Non-FDI	0.19	0.17	0.17	0.19	0.22
Manufacturing	FDI	0.69	0.66	0.92	0.96	0.82
	Non-FDI	0.21	0.17	0.17	0.21	0.24
Services	FDI	0.03	0.06	0.05	0.20	0.07
	Non-FDI	0.06	0.20	0.17	0.11	0.11
FDI-share-wise	10 % - 25 %	0.22	0.13	0.14	0.13	0.13
	25 % - 50 %	0.48	0.36	0.65	0.69	0.50
	50 % & above	0.80	0.76	1.00	1.24	0.96

Source: Based on RBI, "Finances of Foreign Direct Investment Companies, 2011-12", Reserve Bank of India Bulletin, January 2014.

More recent data further suggest that FDI companies pay considerably higher royalties but spend very little on R&D. It also appears that over the years this tendency got strengthened considerably. (Table-5) It is evident from a comparison with the figures reported in the combined Profit & Loss Account that most of the royalties paid were in the form of foreign exchange (more than 85%) outgo whereas more than half of the dividends were paid to domestic entities thereby implying that the ratio of royalty to dividends outgo would be considerably higher than what is reflected in the Table.

Table-3: Rates of Royalty paid by FDI Companies in the Manufacturing Sector

Industry	2010-11	2011-12
Manufacturing	0.96	0.82
Of which,		
- Food products and beverages	0.36	0.38
- Chemicals and chemical products	0.74	0.90
- Rubber and plastic products	0.16	0.19
- Machinery and machine tools	0.66	0.87
- Electrical machinery and apparatus	0.55	0.40
- Motor vehicles & other transport equipments	2.19	2.35

Source: Based on RBI, "Finances of Foreign Direct Investment Companies, 2011-12", *Reserve Bank of India Bulletin*, January 2014.

Table-4: Export-Sales ratios of FDI and Non-FDI Companies

Sector		Export-Sales Ratio (%)							
		2007-08	2008-09	2009-10	2010-11	2011-12	2011-12	2012-13	2013-14
All Companies	FDI	15.4	14.5	11.7	12.3	14.2	12.2	12.2	13.6
	Non-FDI	20.4	19.7	17.3	19.1	21.3	18.6	19.3	20.2
Manufacturing	FDI	13.9	18.7	15.2	15.4	19.3	15.1	16.4	17.1
	Non-FDI	26.7	25.2	22.3	24.5	26.8	23.5	24.5	26.0
Services	FDI	7.9	2.2	0.8	3.0	1.7	3.6	2.1	2.7
	Non-FDI	3.5	5.7	5.2	5.0	5.0	5.8	6.2	5.5
FDI-share-wise	10% - 25%	16.1	16.4	10.3	11.7	11.9	10.3	10.9	11.0
	25% - 50%	9.7	11.7	14.7	14.4	13.7	12.0	13.2	11.2
	50% & above	18.2	15.5	11.3	11.6	16.0	13.7	13.0	16.5
No. of companies covered	FDI	502	533	681	745	766	957	957	957
	Non-FDI	408	388	431	280	406	457	457	457

Source: Based on RBI, "Finances of Foreign Direct Investment Companies, 2011-12", *Reserve Bank of India Bulletin*, January 2014.

Another important aspect of FDI companies' operations in India is that in terms of profitability, there appears to be very little difference between FDI and non-FDI companies at the aggregate level. In the manufacturing sector, however, non-FDI companies generally fared better than FDI companies in terms of profitability measured as the ratio of EBDITA to sales. What is striking is that foreign subsidiaries fared the worst compared to other FDI companies having FDI shares of less than 50%. While at the aggregate level FDI companies fared only marginally better than non-FDI companies, in case of manufacturing companies non-FDI companies were slightly ahead of FDI companies. Within the manufacturing sector, the two sets of companies fared differently in the sub-sectors for which the RBI has reported separate figures. On the other hand, in case of services, FDI companies fared much better than non-FDI companies. Once again a point that needs to be underlined is that within computer and related activities, the difference between the two is somewhat narrower compared to the situation at the overall services. (Table-6)

Table-5: Increasing Royalty Rates and Declining R&D Efforts by FDI Companies

	No. of Companies	Ratio of Expenditure on R&D to Sales (%)	Ratio of Royalty to Sales (%)	Ratio of Royalty to Dividends
2000-01	490	0.32	0.25	0.08
2001-02	490	0.30	0.22	0.06
2002-03	490	0.38	0.22	0.06
2011-12	957	0.09	1.60	0.75
2012-13	957	0.08	1.53	0.66
2013-14	957	0.07	1.88	0.75

Source: Based on (i) RBI, "Finances of Foreign Direct Investment Companies, 2002-03", Reserve Bank of India Bulletin, April 2005 and (ii) RBI, "Finances of Foreign Direct Investment Companies, 2013-14: Data Release", December 3, 2015.

Table-6: Profitability of FDI and Non-FDI Companies

	Company Classification	EBITDA to Sales			Return on Equity		
		2010-11	2011-12	2012-13	2011-12	2012-13	2013-14
FDI-share							
- 10% - 25%		18.0	15.6	15.0	15.0	15.1	15.8
- 25% - 50%		16.5	14.9	14.3	20.0	19.1	19.5
- 50% & above		8.3	6.5	6.3	10.3	9.7	9.7
All FDI Companies (917/957)		13.7	11.6	10.9	13.9	13.4	13.6
All Non-FDI Cos (3,725/4,578)		12.5	10.0	9.4	12.9	12.5	12.1
Manufacturing	FDI	10.5	8.1	7.8	11.1	10.7	11.1
	Non-FDI	12.0	9.4	8.9	11.9	11.3	10.8
Of which,							
- Food products & beverages	FDI	4.6	3.7	4.8	7.8	8.4	9.2
	Non-FDI	4.8	4.7	5.2	8.5	8.4	5.6
- Chemicals & chemical products	FDI	10.1	6.8	8.1	12.5	11.8	12.6
	Non-FDI	7.1	4.0	5.4	12.8	11.8	10.9
- Rubber & plastic products	FDI	20.2	10.2	9.4	13.0	11.2	11.0
	Non-FDI	11.6	8.5	9.5	9.4	11.6	12.5
- Machinery & machine tools	FDI	12.5	9.7	10.4	10.9	10.8	9.9
	Non-FDI	9.1	4.2	-0.3	10.6	10.1	10.4
- Electrical machinery & apparatus	FDI	11.7	7.9	6.6	9.3	7.9	7.7
	Non-FDI	4.6	3.2	2.2	9.2	6.1	6.8
- Motor vehicles & other transport equipments	FDI	8.1	6.2	5.4	9.0	8.8	9.7
	Non-FDI	10.8	10.3	8.3	11.2	9.7	9.2
Services	FDI	20.7	20.9	20.8	20.4	20.9	20.3
	Non-FDI	14.2	11.9	12.2	16.1	16.4	16.2
Of which,							
- Wholesale & Retail Trade	FDI	2.4	1.6	1.9	2.9	4.2	3.9
	Non-FDI	1.2	0.8	-0.7	3.8	4.2	0.1
- Transport, storage & Communication	FDI	17.4	24.3	22.5	7.3	10.6	2.1
	Non-FDI	14.8	6.7	9.3	23.7	20.8	22.5
- Computer & Related Activities	FDI	26.8	26.2	25.9	29.0	28.1	28.5
	Non-FDI	22.1	20.4	21.7	22.3	23.6	25.7

Source: Based on (i) RBI, "Finances of Foreign Direct Investment Companies, 2012-13", Reserve Bank of India Bulletin, January 2015 and (ii) RBI, "Finances of Foreign Direct Investment Companies, 2013-14", Reserve Bank of India Bulletin, December 2015.

Note: Figures in brackets are the number of companies covered in the respective sets of companies.

Diminished Access to Imported Technologies for Domestic Companies

In this context it is also relevant to note that Indian companies could be at a disadvantage in the liberalised FDI regime as foreign companies have generally been unwilling to transfer technologies to unaffiliated manufacturers. Thereby they will have better control over technology and the likelihood of the JVs, if any, being able to use the technologies after the expiry of technology agreements will be an important question. The recent Survey¹² on foreign collaborations by the Reserve Bank of India covering the years 2012-13 and 2013-14 (Tenth Round) provides evidence to this possibility. Even though the Survey results do not explicitly state, it can be deduced from an earlier Survey (Eighth Round) that out of the 866 respondents only 303 had foreign technical collaboration agreements. As many as 160 of these were subsidiaries of foreign investors.¹³ Another 94 were foreign associates.¹⁴ Nine companies had pure technical collaboration and the remaining 40 had less than 10 per cent foreign equity participation and/or had only outward investment. (Table -7) While the description of the last group is ambiguous it also does not rule out the possibility of some of the companies having equity participation by foreign investors through their local affiliates. Further, unlike what the RBI's tabulations suggest, the rights to technology, brand names, etc. might not have been 'transferred' to the Indian subsidiaries/associates. Though these surveys suffer from methodological issues¹⁵, they do uniformly underline that the number of 'pure technical collaborations' agreements is extremely small.

Table-7: Distribution of Companies which reported Technical Collaborations by the extent of Foreign Ownership (Number of Companies)

<i>Company Group</i>	<i>Tenth Round 2012-13 and 2013-14</i>	<i>Ninth Round 2010-11 and 2011-12</i>	<i>Eighth Round 2007-08 to 2009-10</i>
(1)	(2)	(3)	(4)
Subsidiary	160	144	129
Associate	94	83	19
Pure Technical Collaboration	9		10
Others*	40	17	
Total	303	244	158
Number of Foreign Technical Collaboration Agreements	528	334	160
Total Respondents	866	550	*836

* it was explained that 678 companies were having only equity participation without any technical collaboration.

Source: based on the results of various surveys reported by the RBI on its website. Results of the latest survey can be looked up at https://rbi.org.in/scripts/BS_PressReleaseDisplay.aspx?prid=33534

¹² RBI. "Survey on Foreign Collaboration in Indian Industry: 2012-2014 - Data Release", March 24, 2015, available at <https://rbi docs.rbi.org.in/r docs/PressRelease/PDFs/IEPR2009242015.pdf>

¹³ Companies in which a single foreign investor held more than 50 per cent of the total equity.

¹⁴ Companies in which the foreign investors' share holding ranged between 10 per cent and 50 per cent of total equity.

¹⁵ C. P. Chandrasekhar, "Foreign Hand", *Frontline*, August 9, 2013.

With so few companies having 'pure technical collaboration', it can be deduced that in the new regime when restrictions on foreign equity participation have been virtually removed, the scope for independent technology transfer has reduced vastly. In this context it is relevant to refer to the observations of the Prime Minister's Group which said that

In respect of manufacturing sector, almost all subsectors were liberalized and 100% investment by foreign companies was allowed. In fact, the concept of Joint Ventures was also given up.

...

The conditions of divestment to local investors, technology transfer etc., were also given up during this period.

...

The Multinational Companies are ... permitted to open 100 percent owned subsidiaries in India. In other words, in those areas the technology would continue to remain with the Multinational Companies themselves.

...

Purchase of technology is increasingly becoming costly and in view of liberal FDI policies, companies from abroad are reluctant to part with technology even for purchasing.¹⁶

Indeed, according to the latest FLA-FDI Census, out of the 13,669 foreign affiliates as many as 13,456 (98.4%) were unlisted. Again 10,544 (77.1%) of the total 13,669 were subsidiaries.¹⁷

A study conducted for the Ministry of Finance during the initial years of liberalisation brought out clearly the motives of Indian entrepreneurs in seeking foreign partners. In about three-fourths of the cases the Indian partner took the initiative in approaching the foreign party for technology. While the Indian partner moved first to acquire technology, the foreign collaborator preferred the joint venture form of relationship instead of agreeing to provide technology through a pure technical collaboration agreement. The study noted that

This probably would not have been possible if foreign investment was restricted to selected industries as was the case earlier. It seems that liberal investment policies provided the foreign investor a chance to have a stake and possibly control over the venture.¹⁸

The Indian partners' ranking of responses (on a scale of 0 to 5) regarding the factors behind entering into financial collaboration are given in Table-8. There were obvious differences between manufacturing and other companies. The most important reason for manufacturing companies was technology followed by access to international

¹⁶ National Manufacturing Competitiveness Council, *Report of the Prime Minister's Group: Measures for Ensuring Sustained Growth of the Manufacturing Sector*, September 2008, pp 71 & 98. The document is available at <http://nmcc.nic.in/pdf/PMGR.pdf>

¹⁷ RBI, "Census on Foreign Liabilities and Assets of Indian Direct Investment Companies", 2014-15 - Data Release, available at <https://rbidocs.rbi.org.in/rdocs/PressRelease/PDFs/PR13843B19E70119254162A938FB315A52016A.PDF>

¹⁸ S.K. Goyal, et. al., *Foreign Investment Approvals: An Analysis (August 1991 - July 1993)*, Project Report submitted to the Department of Economic Affairs, Ministry of Finance, Institute for Studies in Industrial Development, New Delhi March 1994.

markets. Collaborator's insistence on equity participation followed next whereas availability of foreign funds was ranked much lower. In the case of non-manufacturing companies the highest position was occupied by access to international markets which goes well with the earlier observation that the non-manufacturing group was dominated by export-oriented projects. This view got further strengthened with the evidence presented later in Table - 12.

**Table-8: Reasons for the Indian Partner Entering into Financial Collaboration
-- Manufacturing Companies and Others**

Reasons	Mean Weight	
	Manufacturing Companies	Others
1. Superior technology	4.09	2.77
2. Access to collaborators' international marketing network/exports	3.26	3.50
3. Collaborator preferred equity participation	3.04	3.27
4. Collaborator's brand names & trade marks	2.81	1.77
5. Collaborator's patents	2.63	1.18
6. Availability of foreign funds	2.32	2.36
7. New management & marketing techniques	2.24	1.82

Source: S.K. Goyal, et. al., *Foreign Investment Approvals: An Analysis (August 1991 – July 1993)*, Project Report submitted to the Department of Economic Affairs, Ministry of Finance, Institute for Studies in Industrial Development, New Delhi March 1994.

While the latest Survey on foreign collaboration (2012-2014) suggests that in the manufacturing sector 36.9% of the collaborations were having export restrictive clauses, the real issue is that since the foreign investor being a shareholder in an overwhelming number of cases, restrictions could prevail indirectly through rights written into the Articles of Association and Shareholder Agreements. Having control over management, foreign investors can apply restrictions even without formally incorporating them in the collaboration agreements. The foreign shareholder will be in a position to make most strategic decisions like sourcing of materials and the markets to be served. It is important to note that the RBI is not tabulating the replies to a question in the Survey which asks the respondents to state “[W]hether the use of technology imported through the agreement is allowed after the expiry of agreement?” However, one is aware of such restrictions in case of the joint ventures in defence manufacturing industries (see <http://isid.org.in/wp-content/uploads/2020/05/DN2003.pdf>). Markings on many popular consumer goods clearly indicate that the ownership of the brand names remains with the foreign parent. Payment of lump-sum technical fees might suggest that the paying companies can use the technologies after the expiry of the agreements and in all other cases it is quite unlikely. But it becomes apparent from the Surveys that lump-sum technical fees is less preferred to other forms which either depend solely on royalty payments or a combination of royalties and lump-sum payments thereby implying the long term (even perpetual) nature of the payments -- lump-sum cases are only about one-fourth of the total. (Table-9)

Table-9: Distribution of Agreements According to Mode of Payment of FTC Companies

Mode of Payment	Tenth Round (2012-13 to 2013-14)		Ninth Round (2010-11 to 2011-12)	
	Number	% of total	Number	% of total
Royalty	216	48.1	68	30.4
Both Royalty & Lump-sum technical fees	137	30.5	95	42.4
Lump-sum technical fees	96	21.4	61	27.2
Total	449*	100.0	224	100.0

* Of the 528 agreements, 449 agreements reported the specific mode of payment.

Manufacturing companies with foreign technical collaboration agreements reported negative trade balances, low export orientation (exports to sales ratio was 10.1% in 2013-14) and high import dependence (imports to sales ratio was 25.5% in 2013-14). (See Table-10) For only two industries for which details are available – food products and Electrical Equipment – positive trade balances were recorded in both the years. It was seen earlier (Table-1) that foreign manufacturing subsidiaries were running huge trade deficits. Since technical collaborations are also entered into essentially by companies having foreign equity participation, this provides further evidence to the fact that foreign ownership does not necessarily ensure high export-orientation and positive trade balances.

Table-10: Export Orientation, Import Intensity and Trade Balances of Manufacturing Companies having Foreign Technical Collaborations

Industry	Ratio of Exports to Value of Production (%)		Ratio of Imports to Value of Production (%)		Trade Balance (Rs. Crore)	
	2012-13	2013-14	2012-13	2013-14	2012-13	2013-14
Manufacturing	9.25	10.11	25.81	25.49	-28,580	-28,210
Of which,						
– Food Products	19.14	20.09	12.44	10.68	140	220
– Leather and Related Products	0.44	0.95	7.05	7.62	-150	-140
– Chemicals and Chemical Products	6.03	8.63	12.31	10.95	-490	-210
– Pharmaceuticals, Medicinal, Chemical and Botanical Products	0.00	0.00	14.29	24.32	-200	-270
– Rubber and Plastics Products	6.90	8.23	25.52	24.68	-270	-260
– Fabricated Metal Products, Except Machinery and Equipment	0.73	0.00	100.73	115.50	-1,370	-2,310
– Electrical Equipment	63.29	66.67	45.57	58.85	420	190
– Machinery and Equipment N.E.C.	15.36	26.10	15.11	27.60	20	-120
– Motor Vehicles, Trailers & Semi Trailers	9.70	9.10	10.93	10.27	-780	-790
– Other Transport Equipment	11.14	12.28	12.23	10.83	-90	130
– Other Manufacturing	6.99	7.92	41.75	39.35	-25,810	-24,640

Source: Based on RBI, Survey on Foreign Collaboration in Indian Industry: 2012-2014 – Data Release”, available at <https://rbidocs.rbi.org.in/rdocs/PressRelease/PDFs/IEPR2009242015.pdf>

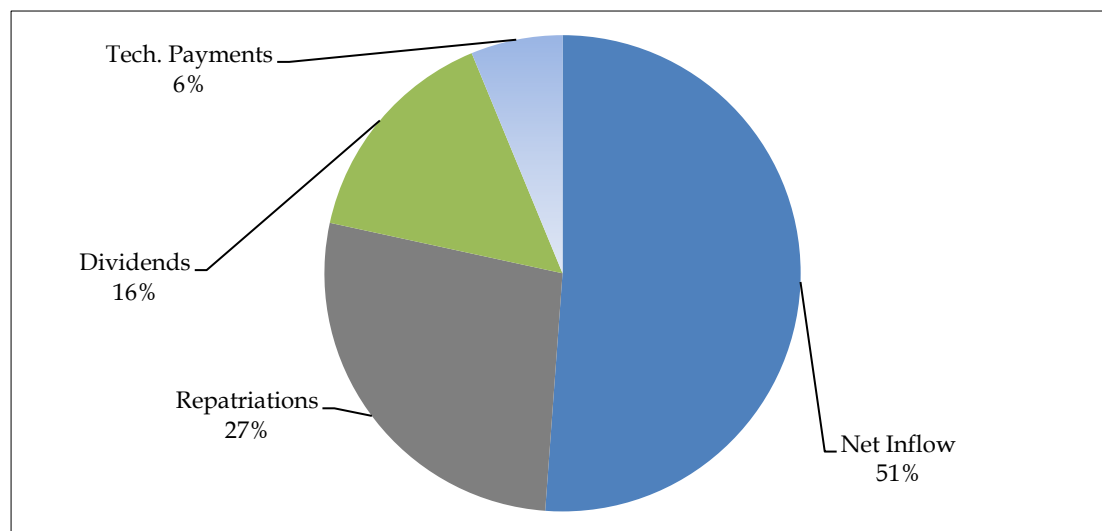
Repatriations add to Adverse Balances on Foreign Exchange Transactions

It was seen in the above that Indian subsidiaries of foreign companies in the manufacturing sector have the tendency to run large trade deficits. In the context of transfer of resources as also earning net foreign exchange there is a need to take the discussion further from the traditional trade and foreign exchange balances. The overall deficit on account of their transactions in foreign currencies including those under other heads like dividend outgo and payments for technology and for other services, could be even higher. There is yet another dimension to their operations which could reduce the resources available for further investment within the economy. Given the fact that the reported FDI consists of investments by a variety of investors, including financial investors who would keep circulating their investments, and M&As, it is evident that actual inflows which could supplement domestic savings and investment and therefore contribute to the economy would be much smaller. Since financial investors seek substantial capital gains within a few years, repatriations are bound to be in multiples of the inflows, for not only do they need not necessarily add to the existing capacities, the outgo on their account results in leakage of domestic resources. Since some of the royalty/knowhow payments could have been made by Indian companies having no FDI, we attributed an arbitrary 50 per cent as the share of FDI companies in the annual outflows on their account. During 2009-10 and 2014-15, outflows due to repatriations, dividends and payments for technology turned out to be a major drain: together they worked out to nearly one-half of the equity inflows during this period. (See Table-11) It is pertinent to note that repatriations/disinvestments alone accounted for more than a fourth of the equity inflows (See the Chart).

Table-11: Ratio of Certain Remittances to Equity Inflows

Year	Gross Equity Inflows (\$ mn.)	Outflows				Ratio of Outflows to Equity Inflows (%) (6)/(2)*100
		Equity Repatriation/ Disinvestment (\$ mn.)	Dividends (\$ mn.)	Charges for Use of Intellectual Property (\$ mn.)	Total (3)+(4)+(5)/2	
(1)	(2)	(3)	(4)	(5)	(6)	(7)
2009-10	27,146	4,241	4,030	2,017	9,280	34.2
2010-11	22,250	6,514	4,901	2,424	12,627	56.8
2011-12	35,854	13,018	5,264	3,207	19,886	55.5
2012-13	22,884	6,853	3,486	4,159	12,419	54.3
2013-14	25,274	4,786	4,041	3,980	10,817	42.8
2014-15	31,885	9,612	3,679	4,820	15,701	49.2
2009-10 to 2014-15	1,65,293	45,024	25,401	20,607	80,729	48.8

Source: Based on the BoP data provided by the RBI periodically based on BPM6.

Chart: Remittances Accounted for Almost One-Half of the Equity Inflows during 2009-10 to 2014-15

Analysis of Transactions of Large Foreign Subsidiaries

To get better insights into the developments described above, we have tried to obtain relevant data regarding a number of FDI companies operating in India in different manufacturing sectors. While in this Paper we shall try to provide a general overview of the empirical evidence, <http://isid.org.in/pdf/WP187.pdf> and <http://isid.org.in/pdf/WP190.pdf> elaborate some of the aspects taking pharmaceutical sector including medical devices and the automobile sector as cases. Though data were collected initially for a large number of foreign subsidiaries and joint ventures with Indian partners, in view of the inconsistencies among the data collected from different sources, it was decided to limit the exercise to foreign subsidiaries for which the data issues are the minimum. The criterion for selection was that the company should have reported a turnover of at least Rs. 500 crore in 2011-12. Particular attention was paid to the inclusion of unlisted ones as coverage of such companies is generally inadequate and most of the foreign companies operate as unlisted private limited companies. Since the issue of dependence on foreign parents for technology is also related to remittances it was felt necessary to look at the companies' R&D efforts in India. The exercise was restricted to foreign subsidiaries because wholly foreign-owned subsidiaries (and the listed ones in which there are no identifiable Indian partners other than public shareholders) would not be constrained/influenced by local partners.

After multiple stages of filtering, the exercise was carried out for 112 foreign subsidiaries. 62 of these are currently listed on the Indian stock exchanges and the remaining 50 are unlisted. There are many other foreign subsidiaries which recorded a turnover of Rs. 500 crore and more. They were, however, not included in this exercise because either they did not have *any* manufacturing activity or, data on all the required aspects were not available in the annual reports downloaded from the website of the

Ministry of Corporate Affairs. We will, however, be referring to such companies at appropriate places. In case of a few included ones, the data has to be reconstructed by referring to related party transactions and entries other than those reported under the heads foreign exchange earnings and outgo.¹⁹ The purpose of this exercise is to provide more empirical and analytical content to the phenomena described above rather than to offer definitive dimensions and ratios.

Providing further confirmation to the earlier observation, the 112 subsidiaries ran substantial deficits both on the trade account as also in terms of net overall earnings in foreign currencies. (Table-12) A noteworthy feature is that at the broad industry level, except for the pharmaceuticals and other transport equipment, all the sectors showed deficits on both the counts. In case of other transport equipment while there was surplus on the trade account, when it came to the overall earnings it too recorded a deficit. Even in case of pharmaceuticals, the surplus was due to Mylan Labs and Fresenius Kabi Oncology -- both were formerly domestic companies but were taken over by foreign companies. The remaining nine companies in the industry ran deficits. It is also relevant to note that 83 of the 112 companies recorded a deficit on the trade account. The number rose to 92 in terms of overall net losses. The trade deficit was the maximum in case of the consumer electronics segment followed by the FMCG sector. Relatively speaking, net losses in foreign exchange terms compared to the trade deficit was high in case of automobiles, FMCG, non-electrical machinery and other transport equipment. The overall deficit was higher by as much as 25% compared to the deficit on the trade account reflecting the relative importance of other forms of foreign exchange spending.

We shall take up the large trade deficit in the case of the FMCG segment for some detailed examination. While Bunge India, which deals in edible oils and which took over the edible oils business of Hindustan Unilever, was responsible for most of the trade deficit of the FMCG segment, only one of the 17 FMCG companies achieved positive trade balance. And none of them achieved net foreign exchange earnings. These include such long established companies like Hindustan Unilever, Bata, Nestle, Mondelez (Cadbury), Procter & Gamble, Glaxosmithkline Consumer Healthcare, Reckitt Benckiser and relatively more recent but large companies like Coca-Cola and

¹⁹ The reporting under these heads did not follow a uniform pattern. Most often the outgo excluded imports. In quite a few cases instead of reporting the data as part of the Directors Report, the user was directed to notes to the accounts or annexures which did not form part of the document. There are issue with regard to the units of reporting (varying as also outright wrong). Since a number of companies were private limited even though the companies might have reported the details in the Profit and Loss account, the same is not available for the public. As a result, data collected initially from the corporate databases had to be rechecked with the actual annual reports and the discrepancies/omissions corrected to the extent possible.

Table-12: Some Indicators of Exports and Foreign Exchange Balances of 112 Foreign Subsidiaries in the Manufacturing Sector: 2011-12

Industry	No of Companies	Trade balance (Rs. Cr.)	Net Earnings in Foreign Exchange (Rs. Cr.)	Exports-Sales Ratio (%)		Share of Service Exports in Total Exports (%)
				All Companies	Excluding Special Cases	
Auto Ancillaries	10	-3,151	-4,218	9.7	9.3	7.7
Automobiles	5	-572	-4,296	16.7	8.3	0.0
Cement	5	-1,512	-1,868	0.7	0.7	15.7
Chemicals Products	3	-302	-478	15.7	15.7	1.9
Basic Chemicals	9	-7,736	-8,114	10.9	10.9	5.8
Consumer Durables	3	-1,032	-1,114	5.4	5.4	33.1
Consumer Electronics	4	-15,932	-17,058	24.2	12.4	11.0
Electrical Machinery	7	-4,890	-4,755	6.9	7.8	6.2
Electronic Equipment & Components	5	-1,755	-2,608	32.6	22.6	34.3
FMCG	17	-15,434	-18,765	15.3	15.5	3.0
Instruments	2	-194	-200	24.2	24.2	59.5
MISC	6	-3,002	-3,414	1.2	1.2	55.8
Non-Electrical Machinery	14	-65	-1,266	17.9	16.9	4.1
Other Non-Metallic Mineral Products	3	-563	-633	6.7	6.7	2.3
Other Transport Equipment	3	151	-886	8.5	9.0	7.0
Paper & Paper Products	2	-4	-20	10.8	10.8	0.0
Pharmaceuticals	11	1,395	1,104	26.1	26.1	2.0
Rubber Products	3	-982	-1,174	1.2	1.2	0.3
All Industries	112	-55,580	-69,762	15.5	27.8	

Source: Based on data collected from Prowess and company Annual Reports.

Hindustan Coca-Cola Beverages. Except two companies, all the companies in the FMCG segment reported payment of some amount of royalty, know-how fee, etc. Bata India, which has been in India since 1931, hardly exports, and its export earnings of Rs. 17 crore do not cover even its payments on account of royalty and know-how, etc. The two companies of the Coca-Cola group reported very small amounts of earnings in foreign exchange. Coca-Cola India reported in its Balance Sheet for the year ending March 31, 2012 as follows.

The operations of your Company do not involve major exports. During the financial year, your Company exported small consignments of non-alcoholic beverage bases to a few southwest Asian countries. Your Company continued its export operations of coffee beans and coffee whitener to South Africa and Kenya. These exports resulted in Foreign Exchange earnings equivalent to Rs.

111 .82 Million Your Company is exploring options to start exporting these products to other countries.²⁰

In fact, out of the Rs. 11.18 crore reported earnings of Coca-Cola as much as Rs. 8.09 crore was 'Service Income'. Only Rs. 3.10 crore was 'Export sales on F.O.B. basis'. Even in case of Pepsico Holdings, which is not covered in this exercise for want of complete information, export-sales ratio was only about 1%. The company explained that "[T]he domestic business of the Company is to manufacture and sell beverages and snacks. The exports business primarily consists of trading in various agro and non-agro products."²¹

In this context one can also refer to companies like ADM Agro Industries (Archer Daniel Midland) which is in edible oil business and which does not figure among the 112 subsidiaries. ADM imported Rs. 376 crore worth of crude oil and its exports during the year were only Rs. 27 crore. The company reported the share of imported raw materials at 84%. Cargill, another major player in commodities uses the services of many local manufacturers. Similar is the case with General Mills which markets Pillsbury brand wheat flour. While it is obvious that a country which faces major deficit in edible oils would import, it needs to be examined what additional benefits the FDI companies would offer India compared to domestic importers especially when they acquire existing companies in the process of establishing themselves in India and also market the products of many unaffiliated local producers.

Some of the companies reported significant amounts of foreign exchange earnings on account of services income. Though in the overall the ratio of such income to export of goods was less than 10%, in some industries it was relatively substantial. In those industries, taking the entire exports as manufactured exports would obviously give a misleading picture. These include technology intensive sectors like consumer durables (33.1%), electronic components and equipment (34.3%) and instruments (59.5%). It is important to note that five out of the eleven companies belonging to these industries are under obligation to export either because they had availed the Export Promotion Capital Goods Scheme (EPCG) or availed benefits which entail export earnings or are located in SEZ/technology parks. The five companies accounted for about 80% of the export earnings of these industries. Overall, 11 such special cases accounted for as much as 38.9% of the exports by the 112 companies and contributed to a little less than one-fourth of the negative trade balance. (Table-13) They also had very high import intensity as seen in terms of the imports-sales ratio. Further evidence to their import intensity can be seen from the fact that in case of Nokia India share of imports in raw materials and components was as high as 84%. In case of Jabil Circuits and Sharp India it was 89% and 75% respectively. Even Philips India which has been operating in India for more than 80 years reported 35% share of

²⁰ Coca Cola India Private Limited, Standalone Balance Sheet for period 01/04/2011 to 31/03/2012, p. 15.

²¹ Pepsico India Holdings Private Limited, Standalone Balance Sheet for period 01/04/2011 to 31/03/2012.

imported raw materials and components. Some of these are also trading in both domestically procured items as also imported finished goods. On the other hand, there are a few large companies in the high technology sector which are merely engaged in trading. We shall discuss about them a little later.

Table-13: Relative Shares of Companies Having Export Obligations

<i>Item</i>	<i>All Companies</i>	<i>Of which, Special Cases</i>	<i>Share of Special Cases (%)</i>
Number of Companies	112	11	
Turnover	4,15,989	91,873	22.0
Exports	64,423	25,128	38.9
Imports	1,20,003	38,194	31.8
FX Total Earnings	69,179	25,989	37.5
FX Total Expenses	1,38,942	41,282	29.7
Net Earnings	-69,762	-15,293	21.9
Trade balance	-55,580	-13,065	23.5
Exports-sales Ratio (%)	15.5	27.4	
Imports-sales Ratio (%)	27.8	41.6	

Source: See Table-12.

A few of the foreign companies operate in India through multiple entities. For a better understanding of their overall operations one needs to study the operations of such entities together. For instance, Glaxosmithkline Consumer Healthcare pays royalty for the use of Horlicks brand to Glaxosmithkline South Asia Pvt Ltd, whose ultimate parent company is GlaxoSmithKline Plc UK. It also purchases goods from the latter. Apart from the payments on a variety of counts to parent company the three main P&G companies in India have substantial transactions among themselves. (Table-14) Incidentally, until 2011-12, the three subsidiaries did not include royalty payments (even though they were shown among the related party transactions) as a part of the foreign exchange outgo. As a result, the popular corporate databases used by scholars failed to include the same in foreign exchange expenditure. Incidentally, Procter & Gamble Home Products explained in the Annual Report for the year 2011-12 that the company made losses because of

1. Introduction of excise duty on Baby care and increase in excise rates for Laundry.
2. Introduction of royalty payments to the parent company.²²

The company paid royalties of as much as Rs. 130 crore during the year. The reported losses were Rs. 353 crore. Another interesting feature of the operations of P&G group companies is that they paid substantial amounts under the head 'Business Process Outsourcing'. The total payments amounted to Rs. 56.25 cr. for the year 2011-12.

²² Procter & Gamble Home Products Limited, Standalone Balance Sheet for period 01/04/2011 to 31/03/2012.

Riello PCI India Pvt Ltd (RPIL) offers another interesting case which is not part of the 112 subsidiaries. The company is a joint venture between RPS S.p.A Italy and PCI Ltd. India, the former's distributor for uninterrupted power supply systems. The foreign investor gradually hiked its stake in the JV to 70%. Annual reports of the company which was incorporated in 2010 reveal that it does not spend any amounts on R&D. RPIL considered the following proposal to pay royalty to the foreign parent. The relevant notice said:

RPIL has established a manufacturing unit at Manesar, Gurgaon in India on the assurance of its OEM partner M/s. RPS S.p.A. that RPS will give support for producing MPT and MHT models in India which were being imported from Italy till now. Now the RPS has agreed to give their support for production of these models.

The technology for producing above models *shall be through PCBs supplied by RPS S.p.A.* who has agreed to supply PCBs to RPIL to produce above UPS models in India.

RPS... has proposed ... to charge Royalty from RPIL on supply of PCBs for above models. The value of the Royalty will be per unit manufactured by RPIL as per duly approved draft of Technology Licence Agreement from RPS, and will be reviewed from time to time keeping in view the market conditions.²³ (emphasis added)

In the following year (2014-15) RPIL paid a royalty of more than Rs. 90 lakhs.²⁴ It did not, however, pay any dividend in order to "conserve resources for growth of the company..."²⁵ It needs to be underlined that royalty is being paid on account of the technology embedded in the *imported PCBs* but *not for manufacturing* those PCBs in India! Incidentally, what role does the junior Indian partner would have in such an arrangement?

To take the discussion on payments for technology (as noted above it is now being referred to as 'payments for intellectual property') further, we have attempted to relate it with payment of dividends. Out of the 62 listed subsidiaries as many as 56 made IP related payments. Further, 48 of these 56 companies paid dividends. All the companies were either making IP payments or paying dividends. On the other hand, 41 out of the 50 unlisted companies were making IP related payments. Only 10 of these 41 were paying dividends. (Table-15) Seven companies made neither type of payments. While only eight of the 62 listed companies did not pay dividends, as many as 31 out of the unlisted companies did not remit dividends. One possible conclusion is that while taking advantage of the royalty payments, the listed companies could not avoid the compulsion of paying dividends. On the other hand, unlisted ones having

²³ Notice to the 4th Annual General Meeting of RPIL to be held on May 14, 2014 downloaded from the MCA website.

²⁴ Due to the poor readability of the document filed with the MCA one could only decipher the figures broadly.

²⁵ Annual Report of Riello PCI India Pvt Ltd, 2014-15, downloaded from the MCA website.

no such obligation preferred to avoid the (costly) dividends route to transfer resources to parent companies.

Table-14: Select Payments by P&G's Three Indian Subsidiaries: 2011-12

<i>Paid by \ Paid to</i>	<i>P&G Home Products</i>	<i>P&G Hygiene</i>	<i>Gillette India</i>	<i>Foreign Parent/ Affiliates</i>
P&G Home Products		<ul style="list-style-type: none"> • Interest Expense • Reimbursement of expenses shared by group cos • Expenses cross-charged 	<ul style="list-style-type: none"> • Interest Expense • Reimbursement of expenses shared by group cos • Expenses cross-charged 	<ul style="list-style-type: none"> • Royalty • Business Process Outsourcing Expenses • Raw materials and stock-in-trade • Assets/Spares • Computer Expenses • Expenses cross-charged
P&G Hygiene	<ul style="list-style-type: none"> • Reimbursement of expenses shared by group cos • Relocation & other reimbursements 		<ul style="list-style-type: none"> • Reimbursement of expenses shared by group cos • Relocation & other reimbursements 	<ul style="list-style-type: none"> • Royalty • Business Process Outsourcing Expenses • Goods • Assets/Spares • Relocation & other reimbursements
Gillette India	<ul style="list-style-type: none"> • Reimbursement of expenses shared by group cos • Relocation & other reimbursements 	<ul style="list-style-type: none"> • Reimbursement of expenses shared by group cos • Relocation & other reimbursements 		<ul style="list-style-type: none"> • Royalty • Business Process Outsourcing Expenses • Goods • Assets/Spares • Relocation & other reimbursements

Source: Annual Reports of the respective companies.

Table-15: Dividends and IP Related Payments by Listed and Unlisted Companies

<i>Type of Company/Royalty Payment Status</i>	<i>No of Companies</i>	<i>Dividend Payment</i>	
		<i>Paid</i>	<i>Not Paid</i>
Listed Companies	62	54	8
- Paying Royalty, know-how fee, etc.	56	48	8
- Not Paying Royalty, know-how fee, etc.	6	6	0
Unlisted Ones	50	12	38
- Paying Royalty, know-how fee, etc.	41	10	31
- Not Paying Royalty, know-how fee, etc.	9	2	7
All Companies	112	66	46
- Paying Royalty, know-how fee, etc.	97	58	39
- Not Paying Royalty, know-how fee, etc.	15	8	7

Source: See Table-12.

Table-16 provides further evidence to the growing importance of IP related payments. It also reflects the relative low spending on R&D. The cases described below help better understand the changing relationships among IP payments, dividends and R&D. Hindustan Unilever Ltd, a foreign subsidiary whose origins in India date back to 1888, decided in 2013 to increase the rate of royalty that it pays to its parent company, that too after the foreign share was increased through buyback. The result is already showing in the pay outs: annual royalty payments doubled from \$57.3 mn

in 2011-12 to \$116.4 by 2014-15. Incidentally, the company started cutting down on its R&D expenditure both in absolute terms and relative to its sales, thus paving the way for continued and greater dependence on the parent. Nestle India Ltd also agreed to hike the rate of royalty paid to the Swiss parent company Nestle SA in 2013. It is relevant to note that Nestle SA has a wholly-owned subsidiary in India called Nestle R&D Centre India Pvt Ltd (earlier Speciality Foods Pvt Ltd) which began R&D operations in 2010. The R&D Centre's objective was reported to be to help Nestle SA

... gain important insights into local consumers' eating habits and taste preferences, as well as great expertise in using and processing local ingredients to develop products for India and beyond ... (Nestle's press release dated Nov 8, 2012)

Table-16: Dividends and Royalty Payments abroad and R&D Expenditures of Select Large Listed Foreign Subsidiaries in India (US \$ mn.)

Year	Nestle India Ltd (inc. 1959)			Hindustan Unilever Ltd (inc. 1933)			Colgate Palmolive India Ltd (Inc. 1937)		
	Dividends	Royalty Payments *	Expendi- ture on R&D@	Dividends	Royalty Payments	Expendi- ture on R&D@	Dividends #	Royalty Payments	Expendi- ture on R&D@
2008-09	40.4	30.0	3.2	144.0	25.6	14.5	21.7	7.0	0.4
2009-10	61.4	37.8	4.3	174.6	18.7	17.8	31.2	15.3	0.7
2010-11	64.6	47.8	4.2	164.0	59.1	20.8	30.7	21.6	1.0
2011-12	55.7	48.9	3.7	157.9	57.3	30.9	33.1	24.0	1.2
2012-13	53.7	52.8	5.7	344.2	68.3	19.2	34.4	26.4	1.8
2013-14	47.4	50.2	6.4	242.7	84.3	12.1	30.7	27.2	2.1
2014-15	60.8	56.4	4.5	314.4	116.4	5.2	27.8	30.1	2.3
Total	384.0	323.9	32.0	1,541.8	429.7	120.5	209.6	151.6	9.5

Source: based on the data provided in Prowess.

* These were calculated from the reported "General Licence Fees" data collected from the company's annual reports. The rupee to dollar conversion rates are those used in the Prowess.

Figures in the brackets in the top row represent the year of incorporation as a joint stock company.

@ Both revenue and capital expenditure.

These were calculated from the reported "Net Dividends remitted" data collected from the company's annual reports for the years 2009-10 and 2010-11. The rupee to dollar conversion rates are again those used in the Prowess.

The main issue, however, is why Nestle India, which has some R&D activity aimed at "testing and modifying of products for local conditions" and which has such a long experience of operating in India was not assigned this task. If this was done, Nestle SA would have had to pay royalties to Nestle India. Instead, The R&D Centre's knowledge would be transferred to Nestle SA to receive which Nestle India would have to pay royalties to its parent. Incidentally, The R&D Centre has been reimbursing expenses incurred by Nestle India on its behalf. The R&D Centre also borrowed substantial funds from Nestle India. The relationship between the two entities needs deeper enquiry as to the nature of research undertaken by the two Indian subsidiaries of Nestle SA. Since setting up the separate R&D Centre, Nestle SA made a direct investment of \$26.38 mn. in it -- far less than the 'General Licence Fees' paid out by

Nestle India during any one of the past seven years. The investment that the Swiss parent made in India has been recovered many times over.

Nestle India's royalty payments are covered under what is termed as General License Fee (again not included by the popular corporate databases under the heads royalty, know-how, etc.).²⁶ The benefits that the company expects to derive from the agreement are described by Nestle India in the following manner.

Your Company has a General License Agreement (GLA) that allows it to access Nestlé Group's intellectual property rights including global portfolio of brands, proprietary science and technology including over 1300 patents, extensive research and development capabilities.

The GLA includes access to over 6,000 brands such as NESTLÉ, MAGGI and NESCAFÉ and technologies developed by the global network of 34 Research & Development facilities, *including one at Manesar, Haryana* which will further assist in localization of global concepts.²⁷ (emphasis added)

Samsung Electronics provides an important example of royalty-paying and profit-retaining companies.²⁸ There is thus a distinct possibility of IP payments being used as a substitute for dividends. The company has been paying royalties on production that depends heavily on imported components. Such payments made by Samsung India to its parent have far exceeded the initial FDI inflows. The company was, however, quite candid in its admission that "Considering the rapidly changing industry scenario; need for further strengthening the business..." it was not paying any dividends. The contribution to India's development made by such enterprises that are perpetually dependent on their foreign parents and incur huge deficits on the trade account since they do not indigenise their production is something that the India needs to take note of.²⁹

In the following we make an attempt to further explore the behaviour of foreign subsidiaries in conducting in-house R&D and payment of royalties. Out of the 112 subsidiaries 37 did not report any R&D. (Table-17) These include some well-known companies which have been operating in India for many decades and which belong to various sectors. Some of the prominent ones are listed in Table-18. Most of these were making some form of IP/know-how payments. Even among those reporting some expenditure on R&D, those who spent at least 1% of their turnover are much fewer – 12 out of 112. Incidentally, only 37 of these were registered with the Department of Scientific and Industrial Research (DSIR) which would have enabled

²⁶ The case of Philips India also illustrates how the databases are finding it difficult to classify multiple forms of payments and the changing nomenclature – Management Support Services, Research and Development Services, Royalty, IT and Communication, Consultation fees and Professional Service Charges and Training – made by the company.

²⁷ Nestlé India Limited, *Annual Report 2014*, p. 27.

²⁸ Biswajit Dhar and K S Chalapati Rao, "India's Current Account Deficit Causes and Cures", *Economic and Political Weekly*, May 24, 2014, vol XLIX, no 21, pp. 41-45.

²⁹ It is also necessary to review the role of independent directors some of whom are highly placed individuals in their respective fields.

them to take advantage of the associated tax benefits -- 7 out of these are in the relatively higher spending range of 1% and above. Whether seen in terms of relative spending on R&D or registration with the DSIR, obviously local R&D is not a priority for the foreign subsidiaries.

Table-17: Distribution of the 112 Foreign Subsidiaries According to R&D Spending and Royalty Payment

R&D-Sales Ratio (%)	Payments for Royalty, Know-how, etc.			Registration with DSIR
	No Payment	Paid	Total	
Nil	6	31	37	2
Less than 0.5	7	35	42	11
0.5 to 1	1	20	21	17
1 and above	1	10	11	7
Not Reported		1	1	
Total	15	97	112	37

Source: See Table-12.

Table-18: Illustrative Cases of Foreign Subsidiaries Not Spending on R&D

Company	Comment regarding R&D/Technology
Atlas Copco India Ltd (1960)	<p>“Since the Company has no specific Research and Development Department, it is not possible to quantify expenditure, whether capital or revenue, incurred on research and development activities.”</p> <p>The company, however, says that:</p> <p>“The Company maintains close contacts with the Atlas Copco Group Companies, which are responsible for the research and development of various product lines. Value engineering and value analysis, with respect to these products, processes and substitute materials, is carried out on a continuous basis to improve quality, reduce rejections and give better value to the Company's customers.</p> <p>The Engineering Competency Centres of the Company, located at Pune and Bangalore, which provide mechanical engineering, CAE and software development services, have been working in close coordination with Product Development Departments of more than 30 group companies all over the world.”</p>
Clariant Chemicals India Ltd (1956)	<p>“The Company during the year 2011 has not carried out any activity which can be construed as Research & Development and as of now there is no specific plan for engaging into such activities in near future. As such, there is nothing to report under this section. “</p> <p>...</p> <p>Technology absorption, adaptation and innovation:</p> <p>“The know-how and technology for the product is made available to the Company from Clariant. The adaptation of know-how and development to cater to the locally available raw materials and suit the requirement of customers for domestic or export markets is done by the Company at its technical laboratories set up at its plants with world class facilities.</p> <p>The Company has not paid any fees for know-how and technology received from Clariant.”</p> <p>The company, however, started paying royalty from 2012 onwards.</p>
Bosch Rexroth India Ltd (1974)	<p>“As no established R & D exists, hence no separate accounts are maintained for such expenditure.”</p>
Coca-Cola India Pvt Ltd (1992)	<p>“Total R&D expenditure as a percentage of the total turnover: Not Applicable”</p> <p>“Technology imported [during the last five years] : N.A.”</p>
Honda Motorcycle &	<p>The Company is a wholly owned subsidiary of Honda Motor Co. Ltd. Japan and the vehicles are manufactured under the technological assistance received</p>

<i>Company</i>	<i>Comment regarding R&D/Technology</i>
Scooter India Pvt Ltd (2001)	from the parent company. Thus as such the Company does not carry out specific R & D in its area of operations.
Honeywell Automation India Ltd (1984)	The company does not refer to R&D in the Directors report but says that HAIL is an affiliate Company of Honeywell International Inc., and on merits it continues to have access to some of the latest products and technology of the parent Company. We continue to roll out new products and technology in the Indian markets as and when they are rolled out in our part of the world.
Honda Cars India Ltd (1995)	While stating that Your Company has been continuously assimilating technology received from its collaborator since its inception. Manufacture of new models and improvements in existing models of cars is done under technical collaboration/guidance of Honda Motor Co.Ltd., Japan. the company merely mentions 'N.A.' against the different R&D expenditure heads.
Lafarge India Ltd (1999)	"EXPENDITURE ON R & D: NIL"
Alfa-Laval (India) Ltd (1937)	The company merely says: The Company has been periodically introducing newer models of decanters, separators and heat exchangers while phasing out their older models for a variety of applications with suitable technological inputs from the Principals.
SKF India Ltd (1961)	Without referring to any in-house R&D efforts, the company says The Company has been consistently supported by its Parent Company, Aktiebolaget SKF (AB SKF) in keeping updated on technology developments. The Company receives technical know-how from AB SKF on continuous basis. This has been used extensively in wide range of products giving competitive edge in the market.

Source: Annual Reports of the respective companies.

The relatively lesser focus on local R&D which was reflected in the studies on Finances of FDI Companies also comes out starkly in case of the 112 subsidiaries. Except for the pharmaceuticals and the miscellaneous industries in all the industries, IP related payments far exceed the expenditure on R&D. The exception in case of pharmaceuticals was due to the takeover of high R&D oriented Indian companies. At the aggregate level IP related payments are more than three times the expenditure on R&D. (Table-19) While most of the companies are more than 10 years old, even those which are in existence in India for more than 50 years are also making IP related payments. (Table-20)

It has been seen that foreign subsidiaries which were investing substantial amounts on R&D were relatively few and those that have opted for registration with the DSIR are even fewer. If taking registration with DSIR as an indicator of the importance and seriousness of the R&D projects, it appears that not many foreign affiliates seek registration with the DSIR. For this exercise we looked at the latest list of individual cases of registrants which had spent at least Rs. 2 crore on R&D projects and tried to identify foreign affiliates among them. Out of the 766 such companies 128 could be clearly identified as having FDI characteristics. Out of the 128, 81 were foreign subsidiaries and the remaining were having Indian partners. Share of the 128 companies in the estimated total R&D expenditure of the 766 companies was approximately 20 per cent. It appears that foreign companies' R&D was heavily

concentrated in pharmaceutical, automobiles and agriculture related industries and services. (Table-21) These sectors accounted for more than 90% of the reported R&D expenditure. If one takes out pharmaceuticals the R&D in which was a legacy of the erstwhile Indian promoters, foreign companies -- whether subsidiaries or joint ventures -- the focus was in just two sectors namely automobiles and components and agricultural inputs.

**Table-19: Industry-wise Distribution of R&D Expenditure and IP Related Payments
(Amount in Rs. Crore)**

<i>Industry</i>	<i>R&D Expenditure</i>	<i>Royalty, know-how fee, etc.</i>
Auto Ancillaries	222	225
Automobiles	391	2753
Cement	9	122
Chemicals Products	36	77
Basic Chemicals	76	128
Consumer Durables	49	52
Consumer Electronics	129	823
Electrical Machinery	82	316
Electronic Equipment & Components	14	318
FMCG	306	1387
Instruments	0	1
MISC	128	87
Non-Electrical Machinery	129	251
Other Non-Metallic Mineral Products	3	28
Other Transport Equipment	0	55
Paper	2	1
Pharmaceuticals	438	79
Rubber Products	0	97
All Industries	2014	6800

Source: See Table-12.

Table-20: Age-wise Distribution of the 112 Foreign Subsidiaries and their Status with respect to IP Related Payments

<i>Age of the Company</i>	<i>No. of Companies Paying Royalty, etc</i>				<i>All Companies (4)+(5)</i>
	<i>Rs. 10 cr. & more</i>	<i>Up to Rs. 10 cr.</i>	<i>Sub-Total (2)+(3)</i>	<i>Nil</i>	
(1)	(2)	(3)	(4)	(5)	(6)
Less than 10 Years	1	2	3	3	6
10 to 20 years	13	11	24	5	29
20 to 50 years	17	15	32	2	34
50 years and above	26	11	37	6	43
Grand Total	57	39	96	16	112

Source: See Table-12.

There is, however, another dimension to foreign companies' R&D activities in India. Some of them have set up separate specialised R&D centres. It was already explained above that Nestle has one such centre in the form of Nestle R&D Centre India Pvt Ltd. Other prominent companies are Honda R&D (India) Private Limited and Novartis Healthcare Pvt Ltd, Alstom Hydro R&D India Ltd, Samsung R&D

Institute India - Bangalore Private Limited, Allergan R & D Centre India Private Limited, Pharmazell R & D (India) Private Limited and Allergan Pharmaceutical Development Center India Private Limited. Probably such separation enables them to attract lesser attention, convenient pricing of services which keeps the R&D centres show minimum profits and extract technology payments from the operating companies.

Table-21: Industry-wise Distribution of FDI Companies Registered with the DSIR

Industry	Foreign Subsidiaries		Joint Ventures		All Companies	
	No. of Cos	Expenditure (Rs. Cr.)	No. of Cos	Expenditure (Rs. Cr.)	No. of Cos	Expenditure (Rs. Cr.)
Pharmaceuticals	24	1,846	2	34	26	1,880
Automobiles	4	1,144	1	222	5	1,366
Auto Components	8	299	28	402	36	701
Agriculture: Seeds, Pesticides, Poultry, etc.	*16	508	4	128	20	636
Non-Electrical Machinery	7	54	5	54	12	108
Consumer Electronics	2	71			2	71
Electrical Machinery	1	5	3	50	4	55
Chemical Products	6	33	2	6	8	39
Consumer Durables	2	38			2	38
Instruments	1	38			1	38
FMCG	4	22	1	15	5	37
Basic Chemicals	5	25			5	25
Research & Development	1	8			1	8
Non-Metallic Mineral Products			1	4	1	4
All Industries	81	4,090	47	915	128	5,005

* Including one company whose entire capital is held by two foreign private equity investors.

Based on DSIR, "List of In-House R&D Units in Industry Reporting Annual Expenditures" available at http://dsir.csir.res.in/webdsir/#files/a_report/english/2014/DSIR_AR_2014-15E.html

Even those who spend on R&D may be doing it as a part of the global strategy of the foreign parent as is evidenced by the following cases.

- **Sandoz India Private Limited**

The Company's Development Centre is one of the global Development centres of the parent company to provide support in the development of speciality and generic pharmaceutical products to cater to the expanding business of the Company. ... The company achieved successful dossier submissions for the US and European projects for a number of formulation and API projects.

The new products and processes developed at the Development Centre are planned to be transferred to any of the manufacturing site worldwide for introduction and launch by the parent or Group Company. The development activities provide a technical support to the parent company as well as to other affiliate companies.³⁰

- **BASF India Limited**

³⁰ Sandoz Private Limited, Standalone Balance Sheet for period 01/04/2011 to 31/03/2012

During the year, your company's Research and Development team was engaged in supporting the technology platforms of BASF, locally as well as globally, with multi-fold activities which include research in the areas of: New organic chemicals intermediates for various applications, Process development and scale up, Agricultural solutions, Textile auxiliaries, Leather chemicals, Other speciality chemicals.³¹

- **ABB Limited**

Considering the nature of research and development, complexity, competence required, time frame, amount and also to optimise overall cost, all major R&D efforts are pooled centrally at the Group level. Company as a beneficiary of these developments has contributed Rs 51 million (excluding refund related to previous year) to ABB Research Limited, Zurich, Switzerland. Localisation of products manufacturing, adoption to local environment and other improvements, cost saving actions are carried out locally. Total expenditure on such development efforts during the year is estimated to be Rs 10 million.³²

While this is a distinct possibility, there are questions about the manner in which the expenditure on R&D is reckoned with. Such a question acquires added significance in the context of many of the companies claiming to be incurring R&D expenditures have not been registered with the DSIR which could have given them the tax benefit. The classification of expenditure on R&D appears to be at the discretion of individual companies rather than based on any accounting or norms prescribed by the government. Another question that crops up is in case of local R&D centres of foreign companies. From the details provided by the companies it appears that the pricing is determined on contractual basis rather than on the benefits that would accrue to the foreign parent. A few relevant extracts from company annual reports are given below.

- **Sandoz India Private Limited**

Revenue from services on time and materials contracts is recognised based on the services provided and billed as per the terms specified in the service contracts. The company follows proportionate completion method of accounting for revenue from services, which is based on the estimates made by the management.³³

- **Makhteshim-Agan India Private Limited (now Adama India)**

Revenue from research and development services is recognised on actual cost plus applicable markup as per agreement with the Group company.³⁴

- **Alcatel-Lucent India Limited**

³¹ BASF India limited, Annual Report 2011-2012, p. 14.

³² ABB Limited, India Annual Report, 2011, p. 16.

³³ Sandoz Private Limited, Standalone Balance Sheet for period 01/04/2011 to 31/03/2012

³⁴ Makhteshim-Agan India Private Limited, Standalone Balance Sheet for period 01/04/2011 to 31/03/2012.

It is relevant to note that the auditors of the company stated that "[I]n our opinion, and according to the information and explanations given to us, there are no contracts and arrangements the particulars of which need to be entered into the register maintained under section 301 of the Companies Act, 1956."

Revenue from software development and related services are recognized based on services rendered and billed on a cost plus basis as per the terms of the respective software service agreements.³⁵

FDI Companies and Profitability

Given the nature of IP related and other payments, a question arises as to the relevance of the usual measures of profitability in case of Indian subsidiaries of foreign companies. It was seen earlier that foreign subsidiaries were the least profitable among the FDI companies studied by the RBI. A useful dimension could be seen in the profitability of listed and unlisted subsidiaries. From Table-22 it can be seen that while relatively more number of listed companies were in the higher ranges of profitability, the converse is true in case of the unlisted ones. Indeed, the performance of some of the large companies including trading ones lends credence to the view that India is being denied its due share of tax revenue some of them even incur losses). (Table-23) Obviously, pure domestic companies do not enjoy 'level playing field'.

Table-22: Distribution of the 112 Subsidiaries according to their Profitability

<i>PBT to Sales Ratio Range (%)</i>	<i>Listed</i>	<i>Unlisted</i>	<i>Total</i>
Loss	3	13	16
Less than 5	8	13	21
5 to 10	15	11	26
10 to 25	34	11	45
25+	2	2	4
All Companies	62	50	112

Source: See Table-12

Table-23: Illustrative List of Large Foreign Subsidiaries Incurring Losses or Reporting Low Profitability

<i>Name of the Subsidiary</i>	<i>Year of Incorporation</i>	<i>Financial Year</i>	<i>Income/Turnover (Rs. Cr.)</i>	<i>PBT/Income (%)</i>
Abbott Healthcare	1997	2012-13	3,205	loss
Acer India	1999	2011-12	2,236	0.5
Adama India	1998	2011-12	529	loss
Adidas India Marketing	1995	2011-12	710	2.0
ADM Agro Industries (Archer Daniels Midland)	2009	2011-12	506	loss
AO Smith India	2006	2012-13	111	loss
Bunge India	1997	2010-11	14,917	1.4
Canon India	1996	2012-13	1,796	loss
Cargill India	1996	2011-12	8,569	loss
Casio India	1996	2011-12	214	1.7

³⁵ Alcatel-Lucent India Limited, Standalone Balance Sheet for period 01/04/2011 to 31/03/2012.

<i>Name of the Subsidiary</i>	<i>Year of Incorporation</i>	<i>Financial Year</i>	<i>Income/Turnover (Rs. Cr.)</i>	<i>PBT/Income (%)</i>
Daikin Airconditioning India	2000	2011-12	1,196	Loss
Dell India	2003	2011-12	7084	loss
Delphi Automotive Systems	1995	2011-12	548	1.0
Epcos India	1976	2012-13	574	loss
Exxon Mobil Lubricants	1994	2011-12	516	1.0
Ferrero India	2004	2011-12	342	loss
Fuji Film India	2007	2011-12	502	0.3
Fulford India	1948	2012-13	215	loss
General Mills India	1995	2011-12	468	2.0
Hewlett Packard India Sales	1997	2011-12	8,729	3.3
Kodak India	1973	2011-12	718	loss
Komatsu India	2005	2011-12	889	1.5
Lenovo India	2005	2011-12	2,836	loss
Levi Strauss (India)	1994	2011-12	742	loss
LG Electronics	1997	2011-12	11,568	3.8
Louis Dryfus Commodities India	1997	2011-12	5,274	loss
Mars International India	1994	2011-12	239	loss
Nike India	2004	2010-11	186	loss
Nikon India	2007	2011-12	738	0.4
Novo Nordisk India	1994	2011-12	570	2.5
Panasonic AVC Networks	1996	2011-12	358	2.8
Pepsico India Holdings	1994	2011-12	6,093	loss
Perfetti Van Melle India	1992	2011-12	1,550	2.7
Rieter India	1995	2011-12	312	loss
SABMiller India	1988	2011-12	2,987	loss
Samsung India Electronics	1995	2011-12	19,535	4.0
Schneider Electric India	1995	2011-12	2,688	Loss (PAT)
Shell India Markets	2004	2011-12	2,987	loss
Solvay Specialities India	2005	2011-12	154	loss
Sony India	1994	2011-12	6,779	3.0
Sulzer India	1988	2011-12	209	loss
Toshiba India	2001	2011-12	955	2.6
UTC Fire & Security India	1981	2011-12	117	loss
Wrigley India	1993	2011-12	385	loss
ZTE Telecom India	2003	2011-12	671	loss

Source: Annual reports of the companies for the respective years.

By Way of Summing Up

The above long narration brought out some important and disturbing dimensions of the operations of FDI companies in India, in particular those of foreign subsidiaries. These covered not only the negative trade balances of manufacturing companies but also payments under a variety of heads which worsen the already large adverse balance. If export of services by manufacturing companies is also taken out, the balances on trade account would work out to be even worse. It should also be noted that a good portion of the exports were a result of export obligations. A relevant question to ask is whether such exports would continue at the same scale once the obligations have been met. Service exports by such companies indicate the country's limitations in manufacturing. It may be noted that foreign subsidiaries in India could achieve an overall positive trade balance mainly due to the surpluses generated by the information technology companies. This is extremely important in the context of India's effort to increase the share of manufacturing in GDP and the 'Make in India' programme. Another factor which demands the attention of the policy makers is that repatriations of all forms accounted for almost half of the equity inflows during 2009-10 to 2014-15 with disinvestments and repatriations (more generally by private equity investors) accounting for as much as 27%. Such high servicing burden not only drains away surpluses from the country requiring even larger capital inflows. The problems arising out of 'addiction' to FDI are not imaginary.³⁶

On the other hand, increasing preference for payments in the form of royalties and other heads, extremely low emphasis on R&D, low profitability or even losses coupled with lesser emphasis on dividend payments, point out to the continued dependence on foreign parents and loss of revenue for the exchequer. There is a stark difference between the behaviour of listed and unlisted subsidiaries and between foreign subsidiaries and other 'FDI' companies. On the other hand, the lack of distinction between or even better performance of 'non-FDI' companies could be due to the liberal definition of FDI and/or lack of export focus and low indigenisation and heavy leakages of revenues by FDI companies. Even when some R&D takes place, it is doubtful to what extent India benefits from it both because of the payments are determined by 'contracts' between the foreign parent and its Indian subsidiary and the outcome of the research goes into strengthening of the global parent which is 'sold' back to the affiliates in India. The various tabulations in this and the accompanying Discussion Note ... suggest that the policy of allowing 100% foreign owned entities has not worked to India's advantage. Indeed the results corroborate the observations of the Prime Minister's group.

³⁶ Jože Mencinger, "The "Addiction" With FDI and Current Account Balance", Working Paper No.16/2008, International Centre for Economic Research, Italy. The fear of addiction was also expressed by some Vietnamese economists.

UNCTAD estimated the loss of revenue to host developing countries resulting from inward FDI through offshore investment hubs at about \$100 bn. It elaborated that “[T]here is a clear relationship between the share of offshore investment in host countries’ inward FDI stock and the reported (taxable) rate of return on FDI. The more investment is routed through offshore hubs, the less taxable profits accrue”.³⁷ While stating the obvious what UNCTAD has done is to place a figure on the possible loss of revenue to the developing countries annually. With bulk of the investment coming from tax havens, the loss for India is self evident. This is in addition to the leakages mentioned above.

One may also refer to the serious concerns expressed by economists belonging to Vietnam’s Central Institute for Economic Management (CIEM), which is under the direct authority of the country’s Ministry of Planning and Investment about the role of FDI in the economy. They spoke against the preferential treatment to foreign investors which resulted in local firms being ‘crushed’ and called for a level playing field. They suspect that by using transfer pricing mechanisms foreign companies declare losses and avoid paying taxes. Observations ascribed to the country’s General Statistical Office reveal that they do not transfer advanced technologies and even though they contributed significantly to the country’s trade surplus, ‘its importance to the country’s overall growth was not high because its exports had little to no added value’.³⁸

There is a remarkable similarity in the views expressed by the Prime Minister’s Group and the approach of China’s ‘Indigenous Innovation’ in respect of advanced technologies. (See Discussion Note.... for relevant citations). Some other aspects of China’s experience are also worth referring to. Theodore Moran explained to the United States-China Economic Security Review Mission how after collaborating with different foreign companies like Bombardier, Kawasaki and Alstom in 2004 and subsequently with Siemens and Mitsubishi for producing trains that could reach 200 kmh China went ahead and built even faster trains.

*In less than four years of “digestion”, CSR (Chinese South Car) mastered and improved what it received from Kawasaki, finally cancelling its cooperation agreement. CSR proceeded further to build trains with a maximum velocity of 300-350 kmh.*³⁹ (emphasis added)

³⁷ UNCTAD, *World Investment Report*, 2015, p. 200.

³⁸ “Vietnam economists warn against addiction to foreign investment”, accessed at <http://www.thanhniennews.com/business/vietnam-economists-warn-against-addiction-to-foreign-investment-24860.html>

³⁹ “Foreign Manufacturing Multinationals and the Transformation of the Chinese Economy: Faustian Bargain to Trade Technology for Access?”, prepared statement of Dr. Theodore H. Moran, Marcus Wallenberg Chair in International Business and Finance, School of Foreign Service, Georgetown University, Washington, DC, in *Chinese State-Owned Enterprises and U.S.-China Bilateral Investment*, hearing before the United States-China Economic Security Review Mission, One Hundred Twelfth Congress, First Session, March 30, 2011.

The problems in extracting technology from the collaborators and the determination with which China's SOEs pursued the acquisition can be seen from the Box-B.

Box-B: No Free Technology Lunches

In January, 2007, Chang [now deputy chief engineer of Changchun Railway Vehicles Co., Ltd, a manufacturing and research subsidiary of China CNR Corp Ltd, a state-owned enterprise which had collaboration with Alstom] led a seven-member work team in a two-month-long training program on train control systems at an Alstom factory in Italy. The team's major task was to learn the mechanisms of the train network control system and its interaction with various sub-systems.

However, Alstom did not include this into the training plan for the visiting Chinese engineers, despite it being stipulated in the contract the two sides signed.

"After several rounds of negotiation, we finally acquired the 3,000 pages of research materials that illustrated the mechanism of the train network control system, but it was in Italian," said Chang. It was the first time Chang had come into contact with the core technology of the world's most advanced MU train. But he[sic] first they had to tackle the problem of deciphering the Italian wording.

For confidentiality reasons, they were not allowed to hire translators. The seven Chinese technicians, who had never studied Italian before, armed themselves with an Italian-Chinese dictionary and cracked the toughest nut of their careers. It took them eight months to read all the materials.

Source: http://www.china.org.cn/china/2016-01/12/content_37557707.htm

In another case, China's Huadian Corp, one of the five largest state-owned power generation enterprises in the country, formed a majority-owned joint venture with General Electric (GE) of the US to manufacture distributed energy resources (DER). According to Huadian's vice manager Deng Jianling this was the

... first step for us to introduce key DER technical equipment from the U.S. In the next stage we will gradually localize the technology.⁴⁰

This was a part of China's plans to launch 1,000 distributed energy projects based on natural gas to provide electricity to consumers located near the plants to minimise transmission losses.

And the US Chamber of Commerce noted:

Indigenous innovation seems to be a policy borne as much of China's fear of foreign domination as China's pride in its great accomplishments and *desire to be a leader in the rules-based international system*.

When it comes to technology transfers, Chinese officials believe foreign companies have been duplicitous and stingy. In their view, the bargain was

⁴⁰ http://www.fdi.gov.cn/pub/FDI_EN/News/Investmentupdates/t20110824_136306.htm

market access in exchange for know-how and technology, and foreign companies *held back their best to contain China's rise*.⁴¹

Again in case of China, based on the study of quite a large number of enterprises, (in which two officials of the National Bureau of Statistics of China also participated) it was found that although FDI contributed substantially to Chinese production and exports “it has not been an important force for promoting R&D investment in domestic firms, which is an important issue in China’s strive towards technological upgrading.”⁴² Another study noted that high levels of overseas investment may also negatively impact on private SMEs by reducing their ability to innovate as it could make it more difficult for them to retain skilled workers, forcing many to cut costs rather than innovate in the face of competition.⁴³

There is extensive literature on the developmental impact of FDI which emphasises the need for focusing on quality rather than quantity. There are equally compelling arguments for strengthening domestic entrepreneurship.⁴⁴ Even for effective spillovers from FDI there is need for capable domestic players. The story of East Asian tigers earlier and China now underlines the need to harness FDI to one’s advantage rather than giving it a free hand. This seems to be the important lesson coming out of India’s experience in the post-liberalisation period. India should start devising a far more relevant statistical system than what exists today.

⁴¹ US Chamber of Commerce and APCO Worldwide, *China’s Drive for ‘Indigenous Innovation’: A Web of Industrial Policies*, pp. 6-7 accessed at https://www.uschamber.com/sites/default/files/legacy/reports/100728chinareport_0.pdf

⁴² Nannan Lundin, Fredrik Sjöholm, Ping He and Jinchang Qian, “FDI, Market Structure and R&D Investments in China”, IFN Working Paper No. 708, 2007, Research Institute of Industrial Economics, Stockholm, Sweden. http://www.ifn.se/eng/publications/wp/2007_4/708_1

⁴³ http://bulletinacademic.co.uk/473_chinese-innovation-stifled-by-fdi-says-study/. A similar view was expressed by Jin Chen of Zhejiang University when he said that overall “MNCs have limited positive effects.” See: National Research Council of the National Academies, Committee on the Competitiveness and Workforce Needs of U.S. Industry, *The Dragon and the Elephant: Understanding the Development of Innovation Capacity in China and India: Summary of a Conference*, 2010.

⁴⁴ See for instance: Stephen D. Cohen, *Multinational Corporations and Foreign Direct Investment: Avoiding Simplicity, Embracing Complexity*, Oxford University Press, 2007; Maria Carkovic and Ross Levine, “Does foreign direct investment accelerate economic growth?”, in Theodore H. Moran, Edward M. Graham and Magnus Blomström, *Does Foreign Direct Investment Promote Development?*, Institute for International Economics, 2005; Manuel R. Agosin and Ricardo Mayer, “Foreign Investment in Developing Countries: Does it Crowd in Domestic Investment?”, UNCTAD Discussion Papers, No. 146, February 2000, http://www.unctad.org/en/docs/dp_146.en.pdf; Ha-joon Chang, “Globalization, transnational corporations, and economic development: can the developing countries pursue strategic industrial policy in a globalizing world economy?”, in Dean Baker, Gerald Epstein and Robert Pollin (eds.), *Globalization and Progressive Economic Policy*, Cambridge University Press, 1998, pp. 97-116; Eric Rugraff, Diego Sánchez-Ancochea, Andy Sumner (eds.), *Transnational Corporations and Development Policy: Critical Perspectives*, Palgrave Macmillan, 2009; Sanjaya Lall, “Reinventing Industrial Strategy: The Role of Government Policy in Building Industrial Competitiveness”, G-24 Discussion Paper Series, UNCTAD, No. 28, April 2004. (<http://www.g24.org/dps28.html>); and Joseph Stiglitz, “Development Policies in a World of Globalization”, paper presented at the seminar “New International Trends for Economic Development” on the occasion of the fiftieth anniversary of the Brazilian Economic and Social Development Bank (BNDES), Rio Janeiro, September 12-13, 2002..