# BOOK REVIEWS

## *Indian Multinationals in the World Economy: Implications for Development*

Jaya Prakash Pradhan
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Outward foreign direct investment (OFDI) from the developing countries, though not a new phenomenon, has grown in volume since the late eighties. And with it, so have the predictable debates on whether or not the phenomenon jells with the received theory of FDI and statistical tests of its impact on the host and home countries. Pradhan's book departs from the beaten track in many ways. Much of the book is based on information and data painstakingly collected by the author from a variety of sources including the financial press in India. The book includes extensive case studies of firms investing abroad, it charts the birth, growth and overseas investments of India's software industry in some detail, and the econometric tests are carefully designed with their limitations acknowledged.

What accounts for the sizeable growth in OFDI from India since the late eighties, with the total stock at the beginning of the year 2006 amounting to $8 billion compared with a stock of $75 million in the year 1986? The obvious answer is that the Indian firms were muzzled in by various sorts of bureaucratic regulations on their operations, including those governing outward FDI. The relatively low levels of investment were mostly in low-technology industries in neighbouring developing countries. The economic liberalization measures, especially the post-1991 measures, that swept away a whole lot of cumbersome rules and regulations, unleashed the pent-up dynamism of Indian entrepreneurs, resulting in the growth of both exports and OFDI. OFDI prior to 1991, the first wave, as Pradhan refers to it, was meagre compared to the post-1990 investments, hardly amounting to 1 per cent of the total stock of $8 billion of overseas investments in the year 2006. The pre-1991 investments were more a flutter than a wave, and there is not much evidence to say that the investments, which were mostly in neighbouring developing countries, were appropriate to the factor endowments of the host countries. A large part of Indian manufacturing industry has always been relatively physical and human-capital-intensive by design and intent of the policymakers. It is the human-capital intensity of industries such as pharmaceuticals, chemicals and machinery and equipment that endowed Indian firms with the so-called ownership advantages, including product differentiation managerial skills and relatively high labour productivity. As Pradhan notes, the emphasis placed on science, engineering and management education for a long time by India's policymakers has paid off in the post liberalization years. The growth in productivity, product differentiation, and increased R&D by Indian firms mostly devoted to restructuring and adapting imported technology and know-how are all fruits of investments in tertiary education in the past dating back to the Nehruvian era.

No doubt Indian firms are equipped to invest abroad, but do they possess advantages far superior to those possessed by firms in the host countries? It is likely that domestic R&D has endowed the producers of science-based products with unique advantages. In engineering skills-based industries, it is the high labour productivity, or to be specific, the low efficiency wage that may have endowed Indian firms with a competitive advantage. Most firms may enjoy a low efficiency wage, not only because of relatively low wage rates in India, but much more so on account of increased labour productivity. The latter is mostly a consequence of both the physical and human-capital intensity of the production process and the growth in organizational efficiency induced by increased competition in the post-liberalization era. The pronounced tendency to acquire existing firms abroad – what Pradhan refers to as the brownfield investments – rather than invest in greenfield ventures may also stem from the organizational and managerial abilities of Indian firms reflected in their high labour productivity. Acquisitions may be motivated by the desire to acquire technology and know-how possessed by the firms that are acquired, but the acquired know-how and technology have to be organized and managed. That which is acquired may be technology embodied in equipment and knowledge embodied in blueprints and designs. This sort of technology and know-how has to be translated into products and processes. It is here that the Indian firms may possess an advantage over others. The fortunes of the acquired firms in the developed countries, principally in the United States and the United Kingdom, may be on the wane mostly because of an inelastic supply of human capital including engineering and science-based skills. Indian firms are able to acquire these firms mostly because of their access to an elastic supply of such skills both in India and in the host countries from India's diaspora.

These advantages the Indian firms possess may be much more pronounced in the software industry than in manufacturing. India appears to possess a comparative advantage in the sort of mathematical skills that software requires. Here again, it is the investment in tertiary education, specifically in science and engineering, that has enabled Indian software firms to operate with a relatively low wage. Pradhan's detailed analysis of the birth and growth of India's software industry identifies not only the contribution of investment in tertiary education, but also state support for the growth of the sector. There are, though, those who argue that the software industry has flourished in India because of the benign neglect of the sector by the state – neglect not by intent but because the bureaucrats had no knowledge of the totally new industry. This may be a harsh judgement of the bureaucrats; they should be credited with providing infrastructure facilities for the sector including technology parks and satellites. The state should be congratulated for facilitating the growth of the sector rather than interfering with meddlesome rules and regulations in the operations of the software firms. Pradhan is right to emphasize the role of various institutions including the state and the firms in the birth and impressive growth of the software sector, but it may be an exaggeration to say that the sector owes its growth to a national innovation system and a theory of innovation and internationalization can be built around it.

The study recognizes one of the vital elements missing in much of the discussion on India's outward investment, namely the role of entrepreneurs. Pradhan's case studies of software firms refer to the role of entrepreneurs in the growth of the sector. The role of entrepreneurs is not confined to software; it is also present in pharmaceuticals, steel and automobiles. This is an aspect of OFDI that cannot be captured in regression equations; it requires detailed case studies of entrepreneurs, analysing the factors that have motivated them and the manner in which they have coped with risks and uncertainty and seized opportunities others have overlooked. These sorts of interdisciplinary studies on Indian entrepreneurship are unfortunately rare.

Apart from the determinants of OFDI, the book also discusses its impact on employment and India's exports, and the implications for future policy. As the study notes, there are a number of statistical studies that detect complementarity between exports and OFDI. Intuition suggests that OFDI would displace exports from the home country of the firms investing abroad. Pradhan, on the basis of a sophisticated econometric model, suggests that "the empirical findings corroborate the hypothesis that OFDI by Indian multinational firms has played an instrumental role in their export performance. The complementary relationship between OFDI by Indian multinationals and home country exports appears to have dominated their substitution relationships" (p. 157). The statistical tests also suggest that relatively young firms are prone to being much more export-oriented than older firms; that the size of firms has a positive impact on exports up to a threshold level; and that indigenous R&D has a positive impact on exports. These results, based on a sophisticated econometric exercise with an extensive database that would be the envy of most researchers, are not all that surprising. The explanation for the complementarity between OFDI and exports is twofold. First, OFDI promotes exports by providing market intelligence to exporters, and after-sales service to customers. Second, OFDI generates demand for components and raw materials from the home country. Whilst both explanations seem plausible, they are yet to be verified. It is also likely that the markets for the sort of goods that Indian firms export are segmented from the sort of markets that firms investing abroad serve. The latter may be for highly differentiated products with a relatively high income elasticity of demand, and exploitation of these markets requires the presence of the producers in the locale of the customers. Here, market intelligence and an ability to respond to differing tastes of customers with differentiated products may be crucial for the success of the firms. The market for relatively cheap homogenized goods, however, may be served by exports. There could, though, be synergies for the exporters from the FDI operations of the firm. Thus, one and the same firm may be engaged in both exporting and production abroad.

Employment creation by firms investing abroad is another aspect of India's OFDI examined in the book. Here again, Pradhan puts his econometric expertise and access to data to good use and arrives at the conclusion that OFDI promotes employment in the home country. It does this by generating demand for raw materials and other inputs from the home country. The explanation for the benign impact of OFDI on employment is much the same as the explanation for its impact on exports. Here again, there is room for much more detailed analysis.

In sum, Pradhan's book caters to varied tastes: to researchers interested in the relevance of received theory for an explanation of the recent growth in India's OFDI; to readers interested in details on the scale, composition and regional distribution of India's OFDI; to those who relish case studies and detailed review of policy; and, of course, to those who savour sophisticated econometric techniques. Pradhan deserves to be congratulated on producing a book which caters to a diverse readership on an important development in India's recent economic history.

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# Multinational Companies from Emerging Economies: Composition, Conceptualization and Direction in the Global Economy

Andrea Goldstein

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There are a number of important questions about transnational corporations (TNCs) from emerging countries. Practically, the questions revolve around the extent and growth of their activity, and whether their impact on host countries is better or worse than "traditional" TNCs from advanced "Western" countries. For theorists, the big issue is how far existing theories of TNCs can explain their operations. In terms of management, are new skills necessary, or can western management techniques be adopted?

Andrea Goldstein's book promises to confront these three questions. Its subtitle is "Composition, Conceptualization and Direction in the Global Economy". The first four chapters after the introduction provide the factual basis – examining Southern outward foreign direct investment (OFDI), industry categorization, "New Asian Multinationals" and "Multilatinas" (TNCs operating regionally across Latin America). Chapter 6 examines existing theories and their relevance to emerging country TNCs (ETNCs). The remaining chapters examine the external impact of ETNCs – the role of governments, impact on financial markets and host economies and companies for OECD governments, firms and workers. Issue of management are dealt with in part of chapter 8 (diaspora entrepreneurship and "the challenge of multinational management"). The preponderance of the book is thus on extent and impact, less on theory and management.

The factual chapters rely on UNCTAD data, although the author has assembled data on, for instance, employment in ETNCs. The chapter on Translatinas is short and sketchy and has been superseded by CEPAL's 2007 Study, *La Inversión Extranjera.*

The chapter on New Asian Multinationals is the most interesting, mixing macro data and case studies to good effect, although it is marred by casual assumption of a "flying geese" model. This chapter and the one on industry structure would have been better placed following a hard look at theory, because an industry categorization would fall out of a theoretical overview. Inevitably, a modified eclectic (OLI paradigm) model is suggested as a theoretical overview. Goldstein categorizes OLI as Why?(O), Where?(L) and How?(I). However a deeper analysis, undertaken in more recent works on ETNCs (Buckley et al. (2007) suggests that a deeper examination of context is necessary. ETNCs respond to market imperfections in the source country, and this reflects their internationalization path, industry structure and choice of location.

Institutions, too, are important determinants of the activities of ETNCs. Goldstein examines source country policies in chapter 7. His analysis is perceptive and illustrates the importance of government policies. The impact on host OECD countries is the subject of chapter 9. The impact is clearly linked to the motivation and entry modes of ETNCs, but this is not a fully worked-out analysis. As we have "far too few data points" on performance (p. 139), it is inconclusive with warnings of the risks of protectionism and the need for proactive strategies leading to a diffuse conclusion.

Issues of management are considered in chapter 8. Expatriate communities are found to be important in the strategies of ETNCs, and the discussion of the challenge of multinational management is promising and could, with profit, have become a full chapter. The same may be said of the short but intriguing section on financial issues – centred on the important question of whether ETNCs overpay for foreign assets. The final section of this chapter on host country effects suffers from a lack of hard evidence.

The conclusion, inevitably, is a plea for more research on this key global phenomenon. Goldstein suggests that there are many missing elements in a so-far incomplete future research agenda. This book is a genuine attempt to pull together extant information in a concise way, and it largely succeeds. It is, however, important that a tighter theoretical perspective be brought to bear. Increasingly, eclectic agendas need to be simplified by the application of simple, powerful analytical approaches that prevent the unnecessary multiplication of concepts.

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