RIS DP# 5-2000

Multinational Enterprises and M&As in India: Patterns and Implications

Nagesh Kumar

Version: 1.1

June 2000

Published in
***Economic and Political Weekly*, 35, 5 August 2000: 2851-8**

Research and Information System for Non-aligned and other Developing Countries,
Zone 4B, Fourth Floor, India Habitat Centre, Lodi Road, New Delhi-11003, India
Phone: 468 2175; Fax: 468 2173;
email: nagesh@del6.vsnl.net.in

This paper is a part of a larger ongoing work on investment and competition policy at the Research and Information System for Developing Countries, New Delhi. An earlier version was presented at the Workshop on Cross-border M&As and Sustained Competitiveness in Asia organized by UNCTAD in Bangkok on 9-10 March 2000. I have benefited from discussions with Dr V.R. Panchamukhi and from the comments of participants. Dr. P.L. Beena helped in preparation of the dataset for this paper. The usual disclaimer applies.

Multinational Enterprises and M&As in India: Patterns and Implications

1. Introduction

Mergers and acquisitions (M&As) have become increasingly important channels of cross-border industrial restructuring and foreign direct investment all over the world. In India, the policy liberalization in the 1990s has facilitated M&As including cross-border M&As. As a result, the M&A activity has boomed over the past few years. In contrast to nearly all of FDI inflows destined to India taking the form of greenfield projects until early 1990s, a substantial proportion of current FDI inflows takes place in the form of acquisition of existing enterprises in the country. The developmental implications of this trend need to be examined and analyzed.

This paper makes an exploratory attempt to map out the recent M&A activity in the Indian corporate sector associated with foreign MNEs and their Indian affiliates. That is attempted with the help of an exclusive database built-up by us that covers most of the deals associated with MNEs in India for the period April 1993 – mid-February 2000. This database helps to examine the industrial composition of the deals as well as their motives. The structure of the paper is as follows. Section 2 briefly summarizes the policy framework governing M&A activity. Section 3 examines the emerging patterns and motives of MNE related M&As in India. Section 4 discusses implications of the MNE related M&As for various parameters of development. Section 5 concludes the paper with some remarks for policies.

2. Policy Framework

The policy and regulatory framework governing the M&As has gradually evolved in the 1990s. Before 1990, an open offer was mandatory for acquiring 25 percent stake in a company. In 1990, this threshold was reduced to 10 percent of a company's capital. However, in case of MNE related acquisitions, provisions of the Foreign

Exchange Regulation (FERA) Act, 1973, also applied which imposed a general limit on foreign ownership at 40 percent. In addition, Monopolies and Restrictive Trade Practices Act (MRTPA), 1969, gave powers to the Union government to prevent an acquisition if it was considered to lead to 'concentration of economic power to the common detriment'. In 1992, the government created the Securities and Exchange Board of India (SEBI) with powers vested in it to regulate the Indian capital market and to protect investors' interests. SEBI also took over the functions of the Office of Capital Issues Controller. Besides as a part of the package of reforms and policy liberalization, the government announced a New Industrial Policy (NIP) in July 1991. NIP accords a much more liberal attitude to FDI inflows. Furthermore, the FERA restrictions on foreign ownership in Indian companies were abolished and requirement of prior government approval on M&As was removed (see Kumar 1998, for more details). In November 1994, SEBI issued Guidelines for Substantial Acquisition of Shares and Takeovers, widely referred to as Takeover Code 1994. However, the experience demonstrated that the Code had lacunas and loopholes to deal with the complexity of the situation. Hence, a Committee chaired by Justice P.N. Bhagwati was appointed in November 1995 to review the 1994 Takeover Code. The Committee's Report of 1996 formed the basis of a revised Take Over Code adopted by SEBI in February 1997. The new Code provides for the acquirer to make a public offer for a minimum of 20 percent of the capital as soon as 10 percent ownership and management control has been acquired. The creeping acquisitions through stock market purchases over 2 percent over a year also attracted the provision of public offer. However, acquisitions by those owning more than 51 percent ownership do not attract the provisions of the Code. The price of the public offer will depend on the high/low price for the preceding 26 weeks or the price for preferential offers, if any. In order to ensure compliance of the public offers, the acquirers are required to deposit 50 percent of the value of offer in an escrow account. Furthermore, the acquirer had to disclose sources of funds. The Code was still being reviewed by the reconstituted Bhagwati Committee. On the basis of its recommendations, the government announced some more amendments to the Code in October 1998. These amendments include revision of the threshold limit for applicability of the Code from 10 percent acquisition to 15 percent. The threshold limit of 2 percent per annum for creeping acquisition was raised to 5 percent in a year. The 5 percent creeping acquisition limit has been made applicable even to those holding above 51 percent but below 75 percent stock of a company (see RBI, 1999, and India, Ministry of Finance, 1999).

In sum, the policy regime in the 1990s has greatly liberalized the possibility of industrial restructuring and consolidation through M&As by removing restrictions under the Capital Issues Control Act, MRTPA and the Companies Act. As a result the M&As have increasingly been employed by Indian enterprises for restructuring and consolidate their operations (see Beena, 1999; Basant, 2000). The new FDI policy and abolition of FERA regulations also facilitate acquisitions by MNEs. Although new regulations in the form of the SEBI's Takeover Code have been evolved, their objective is primarily to protect the interests of minority shareholders. The norms for pricing the issue are meant to check the practice employed by some MNEs to increase stakes in their Indian affiliates at prices much lower than the ruling market prices through preferential issues made in their favour. Many M&As deals which involve companies such as the closely held companies and not listed on the stock markets, besides mergers following mergers of foreign parents, remain outside the scope of the Code. The policy framework in India also does not regulate M&A deals from an anti-trust or competition policy perspective as in the EU and in the US. As a result, a number of MNE affiliates have been able to consolidate their market shares in the country by taking over domestic rivals, as will be seen later.

3. Patterns of MNE Related M&A in India

In tune with the worldwide trend, M&As have become an important conduit for FDI inflows in India in the recent years. Official figures on the relative importance of M&As in total FDI inflows are not published. However, the figures summarized in Table 1 from independent sources suggests that during 1997-99 nearly 40

Table 1: Share of M&As in FDI Inflows in India

Year	FDI Inflows ($ million)	M&A Funds ($ million)	Share of M&A Funds In Inflows (%)
1997	3200	1300	40.6
1998	2900	1000	34.5
1999 (Jan.-Mar.)	1400	500	35.7
Total	7100	2800	39.4

Source: *Economic Times*, 23 December 1998 and 21 June 1999.

per cent of FDI inflows in the country have taken the form of M&As by MNEs of existing Indian enterprises rather than greenfield investments. As indicated earlier, until 1990, almost all of FDI inflows in the country took the form of greenfield investments. To examine the sectoral distribution, motives, patterns etc. of MNE related M&As in the country, a database covering 256 deals entered into by foreign MNEs or by their controlled affiliates in India between March 1993 and 15 February 2000 has been compiled. The main sources of the information are reports in financial media and CMIE's Economic Intelligence Service. The database (hereafter RIS-ICDRC database) defines deals as acquisitions if it involves taking over the operations of a going concern by the acquirer. Merger is defined to cover deals where the identities of enterprises involved are merged. Some of the acquisitions are followed by amalgamation of the acquired entity into the acquiring company. However, such deals are classified as acquisitions. Following patterns emerge from analysis of the database.

Inter-temporal Distribution

Table 2 shows that 224 (i.e. 87 percent) of 256 deals have been concluded since April 1996. It is clear that liberalization of FDI policy besides gradual liberalization of overall policy framework in the 1990s has facilitated adoption of M&A route to enter the Indian market or to strengthen their position by MNEs. A case in point is the takeover by Hindustan Lever Ltd. of Tata Oil Mills (TOMCO) in March 1994 and of Lakme Ltd. in 1995-96 that would not have been easy in the 1980s because of the provisions of MRTPA as all the three companies involved were MRTP companies.

Table 2: MNE Related M&As in India

Year	Mergers	Acquisitions	Total
1993-94	4	9	13
1994-95	-	7	7
1995-96	-	12	12
1996-97	2	46	48
1997-98	4	61	65
1998-99	2	30	32
1999-00 (upto Jan. 00)	5	74	79
Total	17	239	256

Source: Kumar based on RIS Database

Furthermore, as per the definitions adopted, most of the MNE related deals have involved acquisitions rather than mergers.

Industry Composition of Deals

Although the bulk of the deals have taken place in manufacturing, a number of services have gradually become important in the recent years. Table 3 shows that overall 21 percent - and in 1999-2000, 30 percent - of the deals have been in the domain of services. Banking and financial services, advertising and other business services and travel agencies account for a significant number of deals in the recent years especially in the 1999-2000. It is in tune with the worldwide trend of growing international trade and investment in services. It has also to do with the gradual liberalization of the Indian economy that has generated interest of multinational service enterprises to start operations in the country. In particular, multinational service enterprises in business services such as accounting and management consulting, advertising, market research, travel agencies have started to establish a place of business in the country quickly through acquisitions. Annex 1 lists select acquisitions by MNEs in such new services. For instance, in the travel services, Carlson Wagonlit has acquired Ind Travels, Kuoni of Switzerland has acquired SOTC and Sita Travels. In advertising services, the world's largest advertising agency WPP Group plc which already controls Hindustan Thompson Associates (HTA) through its subsidiary J Walter Thompson, and Ogilvy & Mather India, through O&M, has acquired Equus, a domestic advertising agency besides increasing stake in HTA. Bates, another advertising agency has bought out the joint venture partner in its Indian affiliate. In the services such as these, entry through acquisition provides to MNEs access to the client network of the existing enterprise.

Among the manufacturing industries, although non-electrical machinery with 31 deals appears to have a high concentration, it actually is a branch covering very diverse range of machinery and equipment. MNE related M&A deals are highly concentrated in consumer goods industries – such as food and beverages with 25 deals, household appliances, pharmaceuticals and personal care products. These products are highly sensitive to marketing networks and brand loyalties. Hence, MNEs hope to tap the established marketing and distribution networks and sometimes the brand loyalties of acquired enterprises. Building extensive marketing networks is a time consuming process. Hence, it helps the MNEs to quickly establish their market presence. For instance, Coca-Cola while re-entering the country in 1993 acquired Parle, the largest player in the market with several well-established brands and a nation-wide bottling and marketing network. That gave Coke a head start over the rival Pepsi which, even though having entered the country five years earlier in 1988, was still struggling with a 25 percent share compared to market leader Parle's 60 percent. Coke was not only

Table 3: Industry composition of MNE Related M&As in India

Industry	**1993**	**1994**	**1995**	**1996**	**1997**	**1998**	**1999**	Total
Primary								
Plantations	2	0	1	0	1	0	1	5
Industry	**9**	**7**	**10**	**37**	**51**	**25**	**51**	**190**
Food & beverages	5	3	1	4	4	2	6	25
Textiles & footwear	0	0	0	0	1	0	1	2
Metals & metal products	0	0	0	1	0	2	4	7
Non-electrical machinery	1	1	0	7	9	5	8	31
Electrical machinery	2	0	0	2	2	0	3	9
Household electrical appliances and allied	0	3	2	2	0	3	8	18
Industrial chemicals and allied	1	0	1	5	5	3	5	20
Agro-chemicals	0	0	0	3	3	0	2	8
Pharmaceuticals	0	0	1	2	10	2	2	17
Personal care products and household cleaners	0	0	4	4	1	1	2	12
Cement and glass	0	0	0	0	4	0	2	6
Industrial gases	0	0	0	1	4	0	1	6
Lubricants	0	0	0	1	1	2	1	5
Power generation	0	0	0	0	0	0	2	2
Automobiles and shipyard	0	0	0	3	1	1	4	9
Auto components	0	0	1	2	6	4	0	13
Services	**2**	**0**	**1**	**10**	**10**	**7**	**24**	**54**
Banking & financial services	0	0	1	1	5	3	9	19
Advertising, market research and other business Services	0	0	0	6	2	1	2	11
Travel agencies, hotels and transport	0	0	0	1	1	2	3	7
Software, media and publishing	0	0	0	1	1	1	6	9
Telecom	2	0	0	1	1	0	4	8
Misc.	**0**	**0**	**0**	**1**	**2**	**0**	**4**	**7**
Grand Total	**13**	**7**	**12**	**48**	**64**	**32**	**80**	**256**

Source: Kumar based on RIS Database

able to use Parle's bottling and marketing network but even its brands which are still hugely popular and outsell Coke's own brands of soft drinks. Subsequently taking a cue from the entry strategy of Coke, Pepsi has also acquired Duke, a smaller soft drink manufacturer to build its market share. Similarly, Hindustan Lever, the Indian subsidiary of Unilever has acquired Dollops, Kwality and Milkfood to get into ice-cream market with the help of their marketing networks, production facilities in different parts of the country and brands.

A number of deals have also taken place in the automobiles and auto components sectors. This is due to the liberalization of automobile industry for foreign entrants in the 1990s that has led to entry of almost all the leading auto manufacturers in the country. Establishing production facilities for manufacture of cars and setting up a sales and service network is a very time consuming process. Hence, most of the entrants have chosen to acquire existing auto producers or form joint ventures with them. Auto components industry has followed the acquisition route to quickly set up the manufacturing base in the country to cater to the fast developing market for their wares.

Although cement and glass industries are not so much sensitive to product differentiation, MNEs like Lafarge, Saint Gobain are using acquisition mode to set up their bases in the country in view of large and rapidly growing market. Lafarge has acquired a cement plant of Tata Steel in one of the largest deals and is reportedly bidding for several others in different parts of the country to augment its capacity and market share.

Motivations for MNE Related M&As

MNE related M&A deals are predominantly of horizontal nature. Of the 256 deals studied, only 3 could be classified as vertical. All of these three deals related to food and beverages industry. Two cases relate to Coca-Cola taking over its bottlers and another involving McDonalds taking over its processed food vendor.

Horizontal M&As have been classified further by major motive underlying the deals. In 35 per cent of the cases, the acquisition involved buying out local joint venture partner by MNE parent. In 5 percent more cases acquisitions involved increasing stakes in their affiliates or subsidiaries. Thus roughly 40 percent of deals have related to increasing ownership of existing affiliates of MNEs. A typical pattern of entry in

Table 4: Motives for M&As

	Vertical Acquisitions	Horizontal M&As						
Industry	Buyout suppliers or distributors	Buyout joint venture partner	Increase Stake	Entry in Indian market	Extend scope of operation	Following Merger of Parents	Group restructuring	Total
Primary								
Plantations	0	0	0	0	2	0	3	5
Industry	3 (2)	69 (36)	10 (5)	49 (26)	36 (19)	19 (10)	6 (3)	192 (100)
Food & beverages	3	1	0	8	11	1	1	25
Textiles & footwear	0	1	0	2	0	0	0	3
Metals & metal products	0	3	0	1	3	0	0	7
Non-electrical machinery	0	18	2	7	1	2	1	31
Electrical machinery	0	2	0	2	0	4	1	9
Household electrical Appliances and allied	0	9	1	4	3	1	0	18
Industrial chemicals and allied	0	6	3	8	3	0	1	21
Agro-chemicals	0	0	0	1	2	4	1	8
Pharmaceuticals	0	3	2	5	3	4	0	17
Personal care, products and household cleaners	0	2	0	3	5	2	0	12
Cement and glass	0	4	0	2	0	0	0	6
Industrial gases	0	1	1	4	0	0	0	6
Lubricants	0	4	1	0	0	0	0	5
Power generation	0	2	0	0	0	0	0	2
Automobiles and shipyard	0	7	0	2	0	0	0	9
Auto components	0	6	0	0	5	1	1	13
Services	0 (0)	16 (31)	3 (6)	25 (48)	8 (15)	0 (0)	0 (0)	52 (100)
Banking & financial services	0	2	1	12	4	0	0	19
Advertising, market research and other business services	0	6	0	5	0	0	0	11
Travel agencies, hotels and transport	0	0	2	2	2	0	0	6
Software, media and publishing	0	5	0	3	0	0	0	8
Telecom	0	3	0	3	2	0	0	8
Miscellaneous	**0**	**4**	**0**	**2**	**1**	**0**	**0**	**7**
Grand Total	**3** **(1)**	**89** **(35)**	**13** **(5)**	**76** **(30)**	**47** **(18)**	**19** **(7)**	**9** **(4)**	**256** **(100)**

Source: Kumar based on RIS Database

India followed by MNEs has been to set up a joint venture with an established local group that acquires assets, existing facilities and networks of the local partner. After a few years of functioning of the joint ventures and after getting acquainted of working in India, MNE partner starts raising their stake and often end up buying the stake of local partners completely. The cases include most of the automobile MNEs. For instance, Daewoo which had formed a joint venture with DCM Group, Ford with Mahindra & Mahindra, FIAT with Premier Automobiles, General Motors with Hindustan Motors, and Mercedes-Benz with Telco. In all of these cases, local joint venture partners have been eased out by MNE partners nearly completely. It also applies to many other industries including manufacturers of household appliances such as Electrolux, Whirlpool, Timex Watches; industrial machinery manufacturers such as Cummins, Sulzer, Vickers, Yokogawa, Kent-Taylor, Xerox, and to services such as VNU (market research), IBM (software), among other cases.

Thirty percent of all acquisitions relate to entry in the Indian market. However, proportion of new entry related deals in case of services is much higher at 48 percent. It is clear that more of acquisitions in services area have been motivated to establish a presence in the country. In contrast only 26 percent of the manufacturing cases have involved a fresh entry in their lines of business. Here again food and beverages industry has one of the largest concentrations of acquisitions to establish presence in the Indian market. As discussed earlier, the importance of marketing and distribution network for the industry has prompted MNEs to adopt the route of acquisitions.

Eighteen percent of the deals have been motivated to extend the scope of existing operations or their market share. Bulk of the acquisitions of this type have been undertaken by existing MNE affiliates in India which have resorted to horizontal M&As to augment their market presence. Hindustan Lever, for instance, has acquired TOMCO and Lakme to strengthen their presence in edible oils, soaps and personal care products respectively. Smith Kline Beecham Consumer has acquired brands of Jagjit Industries to further consolidate their market position in nutrition drinks market. Glaxo India bought over three pharmaceutical companies of the Biddle Sawyer Group to strengthen their presence in certain therapeutic market segments, Exide acquiring Standard Batteries and Tudor; Electrolux acquiring Intron (Washing Machines); Hutchinson Telecom acquiring a stake in Sterling Cellular to extend its operations to cover Delhi, or ABN-Amro taking over BankAm’s Indian branches to extend its branch network.

Box 1

Unilever's Subsidiaries in India:
Growth and Market Domination through M&As

Unilever has pursued an aggressive M&As strategy in India since the beginning of their business in the country in 1913 to grow and dominate markets. Its early history reveals that in the initial years it took over several companies that were engaged in trade of soaps and merged them. The present flagship subsidiary of Unilever in India viz. Hindustan Lever Ltd. (HLL) is itself a result of a merger of three Unilever companies in 1944. HLL has since actively pursued M&As strategy to grow and expand its range of activities and strengthen its market presence. Even during the years of restrictive policy before 1991, HLL succeeded to acquire a number of smaller enterprises that had run into financial difficulties but nevertheless could add capacity to HLL's activities often initially on lease basis. These include Stepan Chemicals producer of detergents acquired in 1983; Relish Foods engaged in marine products in 1986; Sarif Garments, Ganesh Garments, and Anand Apparels all engaged in manufacture and export of garments in 1986; detergents unit of Union Home Products in 1988; Sivalik Cellulose Ltd which was engaged in processing and packaging of soaps in 1990. Some of these units especially garment exporters and marine products exporters were acquired to earn foreign exchange that provided HLL import entitlements in those years of regulated regime in India.

Following the policy liberalization in early 1990s, policy restrictions imposed on M&As by large and foreign controlled undertakings under FERA and MRTP Act were removed. HLL has since then has aggressively taken advantage of this liberalized environment to strengthen its market presence and regroup and restructure its diversified product portfolio. The M&A profile of HLL and its affiliates in different product segments over the 1990s could be summarised as follows:

Food and Beverages

Mar 1993	Acquisition of Kothari General Foods (by Brooke Bond India, BBIL)	
Jun 1993	Merger of Doom Dooma India (Tea Plantations) (BBIL)	
Jun 1993	Merger of Tea Estates India (Tea Plantations) (BBIL)	
Jun 1993	Merger of Brooke Bond India and Lipton India to form Brooke Bond Lipton India (BBLIL)	
Jun 1993	Acquisition of Kissan Products	(BBLIL)
Jul 1993	Acquisition of Cadbury's Dollops (Ice creams)	(BBLIL)
Mar 1994	Acquisition of Tata Oil Mills Company (TOMCO)	(HLL)
May 1994	Acquisition of Merryweather Food Products	(BBLIL)
Dec 1994	Acquisition of Kwality Ice Creams	(BBLIL)
Apr 1995	Acquisition of Milkfood Ice Creams	(BBLIL)
Jan 1996	Merger of BBLIL into HLL	
Jan 1998	Acquisition of Kwality Frozen Foods	
Dec 1999	Acquisition of Rossell Industries Ltd. (Tea plantations)	(Unilever)
Jan 2000	Acquisition of Modern Foods Industries	

Detergents

Mar 1995	Restructuring detergents and chemicals business with subsidiary Stepan Chemicals and Hind Lever Chemicals
Feb 1996	Acquisition of Vashisti Detergents

Personal Care Products

Jan 1993	merger of Quest International with Pond's India
Oct 1995	Acquisition of Lakme Lever Ltd.
Sep 1996	Acquisition of Lakme's manfacturing facilities
Jan 1998	Merger of Pond's India Ltd. with HLL

The net impact of the above M&As on the market shares of HLL and its associates in different product segments is summarised below

Segment	Market share of HLL or associates		
	1992-3	1996-97	1997-8
Ice Creams	Nil	68.83	74.06
Souces, Ketchups, Jams	Nil	59.96	63.54
Animal Feeds	n.a.	10.82	12.71
Tea	n.a.	20.74	20.52
Coffee	n.a.	5.16	5.90
Glycerin	37.4	39.55	40.93
STPP	44.79	64.77	65.06
DAP	7.85	9.30	8.79
Cosmetics and toileteries	n.a.	56.26	56.49
Dental Hygiene Products	11.20	35.73	41.56
Soaps	19.66	25.32	26.01
Synthetic Detergents	33.12	47.23	46.72
Vanaspati	0.85	12.61	13.90

Source: Kumar based on EIS (1999).

Source: Kumar based on Shiva Ramu (1998), Beena (1999), and media reports.

Seven per cent of the deals have related to mergers of existing affiliates in the country following the merger of parents. These include merger of Hindustan Ciba-Geigy and Sandoz to form Novartis, Glaxo's merger with Borrough's Wellcome, American Home Products with Cynamid and John Wayeth Laboratories to form Cynamid Lederle, merger of Pond's with Hindustan Lever. Another four per cent of the cases have included mergers of existing affiliates of a MNE as a part of group restructuring. This includes a huge restructuring exercise undertaken by various Unilever group affiliates in the country where all tea businesses were first consolidated in Brooke Bond Lipton India (BBLIL) and then merging BBLIL with Hindustan Lever.

Size of Investments

The size of the deals in terms of the amount of consideration is not available for a large number of cases. In many cases, particularly acquisitions of closely held companies the consideration amount is not disclosed publicly. The information on consideration is available for a subset of 87 of 239 cases of acquisitions covered in the database. The size-wise distribution of these 87 deals summarized in Table 5 suggests a highly skewed pattern with top 10 deals accounting for over two thirds of the consideration paid while the smallest 20 deals account for a negligible 0.79 percent of the total. Therefore, the bulk of the acquisitions by MNEs have involved relatively small amounts. It can be expected that a larger proportion of deals for which consideration amount is not reported are smaller deals because larger deals are more likely to attract SEBI mandated public offers and hence reporting of the scale of consideration. Therefore, it can be inferred that MNEs are acquiring smaller and often closely held enterprises in large numbers to establish their presence or to strengthen the scope and coverage of their operations. These deals being low profile neither attract public attention nor regulatory provisions.

Table 5: Consideration Involved in Select MNE Related Acquisitions

	Total Consideration, Rs. Million	% Share
87 Deals	87449	100.00
Top 10 Deals	50371	66.75
Top 20 Deals	6999	80.04
Bottom 20 Deals	773	00.79

Source: Kumar based on RIS Database

Classifying the 87 deals by the type of acquirer, as summarized in Table 6, one finds that, on average, deals involving acquisitions of domestic enterprises by existing MNE affiliates are generally smaller than those involving foreign corporations acquiring local enterprises or foreign parents buying out joint venture partners.

Table 6: Average Size of Acquisition Deals

Type of Acquirer	Number	Amount Rs. Million	Average per deal Rs. Million
Existing MNE Affiliates	19	13661	718
Foreign Corporations	36	37360	1038
Foreign Parents of Existing Affiliates	32	36420	1138
All cases	87	87440	1005

Source: Kumar based on RIS Database

4. Development Implications

Developing countries seek FDI as a bundle of resources to obviate constraints on their industrialization and development imposed by scarcities of capital, foreign exchange, technology, organizational and entrepreneurial resources. It has been argued by us elsewhere that FDI inflows in the form of M&As are of poorer quality than greenfield FDI inflow in general in terms of their domestic capital augmenting potential, spillover benefits, competition and efficiency (Kumar, 2000, forthcoming). Although the developmental impact of different MNE related MNE deals would vary from case to case, in what follows we review the implications of observed patterns of MNE related M&As on different parameters of development.

Economic Growth and Balance of Payments

Economic growth is a function of change in stock of productive capital employed in the country (viz. Δk). Inflows of FDI are welcomed by developing countries in the expectation that they will contribute to growth by adding to the gross domestic capital formation. In general, greenfield FDI inflows do add to the stock of domestic capital investment, FDI in the form of acquisition may or may not lead to change in domestic capital stock. Most immediate consequence of acquisition is change in ownership which may or may not be followed up by additional capital formation. Some times, the payments made by acquirer to domestic owners may be reinvested in some other projects or MNE acquirer may pursue a more aggressive expansion path of the acquired enterprise than would have been possible with domestic or joint venture ownership with funds raised abroad. On the other hand, the payments made may not be reinvested productively and may circulate in speculative activity especially in the case of acquisition through stock markets. In India's case, in about 27 percent of the cases, acquisitions have been made by Indian affiliates of MNEs, often with their internal fund accruals and domestic borrowings as in the case of acquisition of TOMCO, Lakme, Kissan Products, Kothari General Foods, among others, by Hindustan Lever. Hence, little additional capital inflow and investment may be involved. However, the profits resulting from the new acquisitions will be repatriated to the foreign parent in proportion of the ownership as dividends.

Furthermore, even foreign MNEs have sometimes resorted to leveraged buyouts in India through funds raised from domestic banks and long term financial institutions. For instance, Lafarge has funded its Rs.5500 million acquisition of TISCO Steel in November 1999 with a Rs. 2150 million borrowing from a consortium of domestic financial institutions viz. ICICI (providing Rs.1250 million) and the State Bank of India and HDFC Bank providing the rest. Similarly, Electrolux AB's acquisition of a 74 stake in its venture to take over Voltas' white goods business in October 1998 for Rs. 1600 million was also funded by ICICI with a Rs. 1000 million loan (*Economic Times*, 27 December 1999). Therefore, some of the largest deals involving acquisitions by MNEs have led to a much smaller amount of capital inflow from abroad than it appears from the size of the deals.

Inflow of Knowledge and Technical Efficiency

Greenfield FDI also brings with it new production, organizational and management know-how. FDI in the form of acquisition may also lead to some inflow of knowledge particularly managerial know-how. However, the extent of knowledge inflow per unit of investment is expected to be much higher in the case of greenfield investments than FDI through M&As. Furthermore, the knowledge spillovers which are considered to be important sources of diffusion of knowledge brought in within the host economy are again likely to be higher for greenfield investment compared to acquisition on a per unit basis.

Patterns of MNE related M&As observed above suggest that in a large number of cases, MNEs and their affiliates have acquired running and profitable enterprises. It has not been possible to examine the effect of change in management practices and or production technology with acquisition of enterprises. It is also possible that in some cases, efficiency may actually have declined because of a possible inappropriateness of new management practices or technology in the Indian context. For instance, Coke which acquired Parle Products and its brands in 1993 now has 50 percent of the market share compared to 60 percent for Parle in 1993. Entry of Coke has actually helped rival Pepsi to gain its market share from 25 percent in the time of Parle to 48 percent now.

Furthermore, 40 percent of cases of MNE related acquisition have involved raising stake in their existing affiliates by buying out their joint venture partners, as observed above. In these cases, inflow of knowledge may at best be very limited. In fact, one important conduit of knowledge diffusion may cease to exist with the easing out of local joint venture partners.

Market Structure and Competition

A greenfield investment by virtue of new entry increases competition. However, M&As most often lead to increase in concentration by reducing the number of active enterprises in the market. The patterns of MNE related M&As shows that concentration has increased in many cases. As observed earlier almost all of MNE related M&As have been of horizontal nature. Very often existing MNE affiliates have used M&As to extend market share. Absence of anti-trust or competition law in the country has meant that even MNE affiliates having dominating market position have also resorted to horizontal acquisitions. For instance, Smith Kline Beecham Consumer Healthcare which dominates the Indian market for health drinks with Horlicks (with 54 percent share) and Boost (another 10 percent share) has acquired two brands of health drinks namely Maltova and Viva belonging to Jagjit Industries Ltd. Furthermore, very often MNEs or their affiliates have acquired more than one producer of a product and have consolidated them. For instance, Hindustan Lever group companies have acquired three ice-cream makers viz. Dollops, Kwality, and Milkfood; Kothari General Foods, Kissan Products, and recently, Modern Industries in processed food products, Lipton, Brooke Bond, Tea Estates India, Doom Dooma and Rossell in tea business and plantations (see Box 1). Similarly, Exide has acquired Standard Batteries and Tudor to further consolidate its dominant position (with a 50 market share) in storage batteries. Gillette which started in India by acquiring Indian sharing Products has taken over Wikinson and Harbanslal Malhotra, thus creating a near complete monopoly in the shaving products market; Henkel has acquired Spic Fine Chemicals, Calcutta Chemicals and Detergents India, all producing detergents. Tecumseh has acquired SIEL Compressors as well as Kelvinator's compressor unit. In services GE Capital has acquired, SRF Finance, Country-wide Consumer, Escorts Finance, Maruti Country-wide Auto Finance. As observed earlier, WPP Group in advertising and Kuoni in travel agency business have acquired more than one leading players in their fields. It is clear, therefore, that the pattern of MNE related M&As has led to increased concentration in their market segments.

Box 2

Household Appliances Sector:
MNEs adopt M&As to enter and consolidate

Two MNEs in the household appliances segment viz. Whirlpool and Electrolux have employed similar strategies for entry and consolidation in the country. They have acquired more than one domestic manufacturers and forming joint ventures to gain entry and consolidate their hold over the market quickly.

Whirlpool entered India in July 1994 when it acquired a 51 per cent stake in a joint venture formed with the TVS Group. In February 1995 it acquired Kelvinator of India, the existing manufacturer of refrigerators, to get into this segment. It was later renamed as Whirlpool of India. In February 1996, Whirlpool bought over 27.5 per cent equity of the TVS Group in its joint venture in a move towards assuming a complete control over it.

Similarly, Electrolux started of in January 1995 with acquisition of Maharaja International, a domestic manufacturer of household appliances. In June 1995, it acquired Intron Ltd. a manufacturer of washing machines that had run into financial difficulties. In October 1998, it acquired 74 stake in Electrolux Voltas Ltd. a joint venture that took over the white goods business of Voltas Ltd. (a Tata group company). In December 1998, it bought over the 26 per cent ownership held by Voltas in the joint venture and took complete control of it.

Source: Kumar based on RIS Database

Mergers of MNE affiliates in India following mergers of their parents also contribute to increasing concentration. For instance, merger of Indian affiliates of Glaxo, Wellcome and SmithKline would create in India a company with Rs 19.4 billion turnover, by far the largest in the industry with a combined market share of 7.38 per cent and market leadership of many therapeutic segments.

Furthermore, quantitative studies have shown that MNE affiliates in India generally constitute different strategic groups than their local counterparts with larger scales of operation and follow a different mode of rivalry. Hence, they are protected by mobility barriers from existing local as well as potential competitors (see Kumar 1990). It appears that with the aggressive approach adopted by some of them towards M&As, the gap between MNE affiliates and domestic enterprises will widen even more. In other words, indirect effect on concentration through contrived entry barriers is also likely to be significant.

Employment

MNE related acquisitions are likely to affect employment adversely because with acquisition, MNEs may introduce labour saving managerial techniques they are familiar with. Acquisitions of multiple units and their mergers may make a number of jobs such as those in marketing, finance, administration and other overheads, redundant. On the other hand, greenfield entry nearly always will create new jobs. In India, labour legislation protects workers. However, managerial workforce does not enjoy such protection. There are reports that group restructuring processes undertaken by MNEs after acquisitions are leading to job losses. For instance, restructuring undertaken by Coke by taking over its bottlers has already resulted into loss of 100 jobs (*Economic Times*, 22 January 2000).

5. Concluding Remarks

This paper has made an exploratory attempt to examine the patterns of MNE related M&As in India in the 1990s with the help of an exclusive database. The liberalization of policy framework since the early 1990s has led to MNEs increasingly using M&A route to enter and strengthen their presence in the country. In the recent years two fifths of all FDI inflows took the form of M&As compared to virtually all of FDI inflows coming for greenfield ventures. The bulk of the deals relating to MNEs examined have materialized since 1996 and have involved acquisitions rather than mergers. An increasing proportion of MNE related M&As are in the field of services where multinational service enterprises are seeking to establish a place of business in the country by acquiring established domestic enterprises and their networks. In particular increasing interest of MNEs in financial services, advertising, travel agencies and other business services is notable. Consumer goods industries such as food and beverages, household appliances, pharmaceuticals and personal care products, automobiles have a high concentration of MNE related deals. This is because of the importance of a country-wide marketing and distribution and service network for these industries. MNEs have sought to save time and resources to establish such networks on their own.

The deals relating to MNEs are predominantly horizontal rather than vertical in nature. Two fifths of them involve buying out the local partners in join ventures set up in India or raising their stake. A considerable proportion of the deals, especially in the services, has been motivated to enter the Indian market and establishing a place of business. Extending the scope of operations or consolidation of market share has also guided about a fifth of the cases. Ten per cent of the deals have involved mergers of foreign affiliates following the merger of their parents or as a part of the group restructuring. Size wise distribution of the deals is highly skewed. The bulk of the deals involve acquisition of relatively smaller and often closely held enterprises that evade public attention and regulatory scrutiny.

In terms of development implications, FDI inflows in the form of M&As are generally of an infererior quality compared to greenfield investments. This is because, M&As do not always augment stock of productive physical capital in a host country that contributes to the growth. Some of the acquisitions are actually funded by locally raised resources and actually lead to pretty little inflows. The inflow of knowledge per unit of capital in case of FDI through M&A is also likely to be smaller than for a greenfield investment. The latter also has greater prospects of knowledge spillovers. Furthermore, knowledge inflow in the case of acquisitions of existing affiliates may be rather small. In terms of effect on competition too, green field investments score over M&As as the former increases and the latter generally reduces competition. The absence of an anti-trust regulation in India in the 1990 has allowed even MNEs or their Indian affiliates acquiring their domestic rivals despite their market dominance. Hence, levels of concentration in Indian industry have increased over the past decade.

These findings, therefore, emphasize an urgent need for adopting a comprehensive competition policy framework in India. India had adopted the Monopolies and Restrictive Trade Practices Act way back in 1969. However, that Act is outdated in the current setting. The main focus or emphasis of the Act is on prevention of concentration of economic (as opposed to market) power to the common detriment among other objectives. Hence, the Act required a special scrutiny of all investment applications from large industrial houses and FERA companies under its provisions. Therefore, the Act was perceived to discourage private investments. In the current era when private investments are expected to provide the main stimulus to growth, such provisions seemed counterproductive. Hence, as a part of the reform of industrial policy in 1991, the key provisions of the MRTP Act were repealed. What is left of the Act after the amendment is an emasculated version that can only redress certain complaints of restrictive or unfair trade practices. Hence, the country needs a comprehensive and effective competition law specially designed for the changed domestic and international context.

The need for competition policy becomes particularly critical in a liberal FDI and industrial investment policy regime (UNCTAD, 1997:211). India has gradually liberalized her investment regime and screening mechanisms have gradually given way to automatic approvals of investments fulfilling notified criteria. Furthermore, the global industrial restructuring in the form of M&As among the large MNEs has implications for market structures in the country, as shown above. Therefore, a competition policy needs to be so designed so as to deal with possible anti-trust implications of overseas mergers for India as well besides dealing with M&As of Indian enterprises. Anti-trust laws of many countries include provisions for examining the possible impact of overseas M&As for the country even if none of the participants in the deal belongs to the country and provide for remedial measures to deal with them. The examples include US, EU, Canada, Germany and Mexico (see UNCTAD, 1997, Chapter V, for examples).

There is also a development dimension of the competition policy. The competition policy in a developing country especially in a liberalized regime for trade and investment could also provide a level playing field for domestic enterprises *vis-a-vis* subsidiaries of MNEs which enjoy access to their parent’s brand and trade names besides a number of other intangible assets. To use their advantages most effectively, MNE affiliates tend to adopt non-price modes of rivalry dominated by a heavy reliance on advertising and product differentiation. These strategies raise barriers for the entry of new firms and are referred to as ‘contrived entry barriers’ in the industrial organization literature (see Kumar, 1990, 1994). In order to promote a healthy competition between local firms and MNE affiliates, the competition policy could take the form of either offsetting the monopoly power of MNE affiliation and foreign brands through fiscal measures or assisting national firms to build their own brands and technological capability.

A competition policy for India for the changed domestic and international realities, therefore, will suitably incorporate different dimensions to promote a healthy and fair competition that is so important for achievement of economic efficiency.

Annex 1: Select Acquisitions in New Service Industries

Acquirer/Bidder	Target	Nature	Date	Industry	Motive
WPP Group plc	Equus	Acquisition	Jun-96	Advt agency	Entry in Indian mkt
McCann-Erickson Worldwide	McKann-Erickson dia	Acquisition	Mar-98	Advt agency	Buyout jv partner
WPP Group plc	Hindustan Thompson Associates	Acquisition	Jun-98	advt agency	Buyout jv partner
Bates Worldwide	Bates Clarion	Acquisition	Jan-00	advt agency	Buyout jv partner
Carlson Wagonlit	Ind Travels	Acquisition	Aug-99	travel agency	Entry in Indian mkt
Kuoni, Switzerland	Sita Travels	Acquisition	Jan-00	travel agency	Entry in Indian mkt
Kuoni Travel	SOTC	Acquisition	May-97	travel agency	Increase stake
Jardine Flemming	Karvy Consultants	Acquisition	Apr-96	business services	Entry in Indian mkt
Coopers & Laybrand	SB Billimoria	Acquisition	Jun-96	business services	Entry in Indian mkt
Ernst & Young	SR Batliboi	acquisition	Jan-97	business services	Buyout jv partner
Watson Wyatt	Wyatt India Pvt Ltd	Acquisition	Mar-98	business services	Buyout jv partner
Macmillan UK	Macmillan India	Acquisition	May-97	publishing	Increase stake
McGraw Hill	Tata McGraw Hill	Acquisition	Apr-96	publishing	Buyout jv partner
Polygram International Holding Bv.	Polygram India	Acquisition	Jun-99	publishing	Buyout jv partner
Baring India Investments, Mauritius	BFL software	Acquisition	Jun-98	software	Entry in Indian mkt
Baring Private Equity Partners (India)	Synergy Log-In Systems	Acquisition	Apr-99	software	Entry in Indian mkt
Martek Holdings Incorporation	Mascon Global Ltd	Acquisition	Jul-99	software	Entry in Indian mkt
IBM	IBM Global Services	Acquisition	Sep-99	software	Buyout jv partner
IBM	Tata IBM	Acquisition	Sep-99	software	Buyout jv partner

Source: RIS-ICDRC Database

References

Beena, P.L., 1998, 'Mergers and Amalgamations: An Analysis of the Changing Structure of Indian Oligopoly', PhD Dissertation, Centre for Economic Studies and Planning, Jawaharlal Nehru University, New Delhi.

Basant, Rakesh, 2000, 'Corporate Response to Economic Reforms in India', *Economic and Political Weekly,* February 2000, forthcoming.

EIS (Economic Intelligence Service), (various dates) *Monthly Review of the Indian Economy*, Bombay: Centre for Monitoring Indian Economy.

EIS (Economic Intelligence Service), 1999, *Industry: Market Size and Shares, August 1999*, Bombay: Centre for Monitoring Indian Economy.

India, Ministry of Finance, 1999, *Economic Survey 1998-99*, Delhi: Government of India Press.

Kumar, Nagesh, 1990, 'Mobility Barriers and Profitability of Multinational and Local Enterprises in Indian Manufacturing', ***Journal of Industrial Economics*** (Oxford: Basil Blackwell), 38(4), 449-63.

Kumar, Nagesh, 1994, *Multinational Enterprises and Industrial Organization: The Case of India*, New Delhi, Thousand Oaks and London: Sage Publications.

Kumar, Nagesh, 1998, 'Liberalisation and Changing Patterns of Foreign Direct Investments: Has India's Relative Attractiveness as a Host of FDI Improved?', *Economic and Political Weekly*, *33(22)* 30 May: 1321-29.

Kumar, Nagesh, in collaboration with John Dunning et al. (1998) *Globalization, Foreign Direct Investment and Technology Transfers: Impacts on and Prospects for Developing Countries,* London and New York: Routledge.

Kumar, Nagesh, 2000, forthcoming, *Globalization and the Quality of Foreign Direct Investment: An Empirical Analysis of the Role of Multinationals in Industrialization, Export-expansion and Innovation in Host Countries*, London and New York: Routledge and UNU Press.

RBI, (1997-98) *Report on Currency and Finance,* Volume 1, Mumbai: the Reserve Bank of India.

Shiva Ramu, S. (1998) *Corporate Growth Through Mergers and Acquisitions*, New Delhi, Thousand Oaks and London: Sage Publications.

UNCTAD, 1997, *World Investment Report 1997: Transnational Corporations, Market Structure and Competition Policy,* New York and Geneva: UN

UNCTAD, 1998, *World Investment Report 1998:Trends and Determinants*, New York and Geneva: UN

UNCTAD, 1999, *World Investment Report 1999: Foreign Direct Investment and the Challenge of Development,* New York and Geneva: UN.