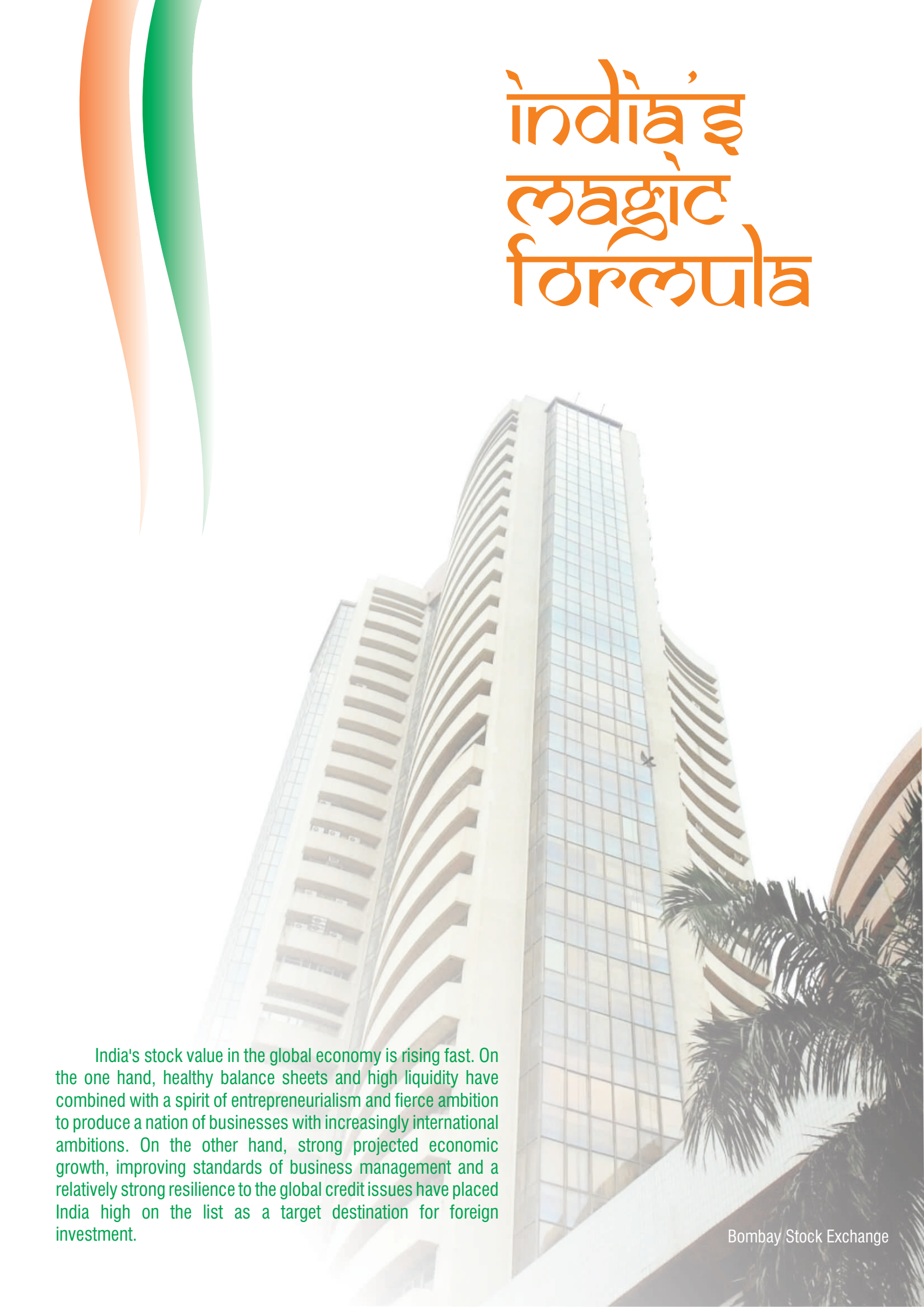




India's Lagging Formula



India's stock value in the global economy is rising fast. On the one hand, healthy balance sheets and high liquidity have combined with a spirit of entrepreneurialism and fierce ambition to produce a nation of businesses with increasingly international ambitions. On the other hand, strong projected economic growth, improving standards of business management and a relatively strong resilience to the global credit issues have placed India high on the list as a target destination for foreign investment.

Destination India

Looking firstly at inward investment, there can be seen a dramatic rise in the volume and value of Foreign Direct Investment (FDIs) into India over the course of the last five years. According to the Department of Industrial Policy & Promotion, a part of India's Ministry of Commerce and Industry, the financial year 2005-06 saw a total of \$8.9bn FDI equity inflows to India. The following year, this figure had soared to \$22.8m, representing a massive 146% rise over the previous year. The level of FDIs continued to rise the following year, with \$34.4bn injected into the Indian market (a 51% annual rise) and even in the midst of a global recession, FDIs only dipped by just 2%, with \$33.6bn invested in the market.

The UK has been responsible for 8% of FDI into India since 2001

Looking at the geographical source of these funds, the UK emerges as the second most active investor behind the US. Between 2001-09 the UK made a total equity FDI of \$5.2bn, representing 8% of total FDI to India over the same period. Given its monolithic status in the world arena you would expect the US to have far outstripped the UK in terms of FDI, but this is not the case. Over the period 2001-09, the US made \$6.3bn of FDI into India.

Furthermore, the total value of FDIs is likely to be substantially higher than these figures suggest. The regulations governing investment in India create an obstacle for foreign investors in the form of the Permanent Establishment requirement, which imposes an almost punitive tax burden on foreign companies. It is for this reason that the majority of investors re-route their investment via funds managed in the tax-haven of Mauritius. For the period 2001-09 FDIs from Mauritius accounted 44% of the total FDI in India, a figure of \$36.8bn. And you can guarantee that a sizeable chunk of this will have originated from UK investors.

Indian Investment Sector Profile

So where is all this money heading? In terms of the sectors that have historically attracted the highest FDI equity inflows, between 2000-09, the services sector (including both financial and non-financial services) secured a total of \$84bn, computer software and hardware \$9bn, telecoms \$6.3bn, housing & real estate \$5.5bn and construction activities (including roads and highways) \$5.2bn. This gives a clear picture of India's business landscape, one where high-tech industry has risen in prominence, and has prompted a need for investment in infrastructure, housing and regeneration, and this in turn has engendered a mammoth support services industry.

What makes India so attractive is that, as an emerging market, it promises immense growth opportunities for savvy investors that make inroads in the right sector at the right time. To quantify this, Reuters has calculated that Indian companies have enjoyed an average economic expansion of 8.6% per annum since 2005. And GDP projections estimate a GDP growth of between 4% (according to the World Bank) and 8% (Dr Pronab Sen, India's Chief Statistician). Little wonder that India is being courted by no fewer than 60 international private equity groups, not to mention the 100+ domestic fund managers



Out of India

India is a prime business destination for foreign companies but what can be said about its own expansionist aspirations?

Nirmalya Kumar, professor of marketing at London Business School has pointed out that as recently as 2001, Indian outward investment was less than \$1bn. However, by 2006 Indian outward investment of \$10bn had outstripped foreign investment into the country. This continued the following year with Indian companies undertaking \$21bn in 40 foreign investment deals in January and February of 2007 alone. Furthermore, Indian foreign investment in the financial year ending March 2007 exceeded the cumulative total foreign investment by Indian companies in the 58 years between its independence in 1947 and 2005.

Looking at the the sectors overseas that proved most popular with Indian companies, according to the Economic Times of India, manufacturing proved to be the most attractive industry, closely followed by the non-financial service sector. Within the manufacturing sector, a wide variety of investments were made, particularly in the areas of electronic equipment, fertilisers, agricultural (and related products) and gems and jewellery, while within non-financial services, investments were principally targeted at the telecoms, medical services and software development services sectors.

Whilst current data demonstrates a drop in India's outbound investments - reflecting the wider state of the global economy and mirroring the sharp decline in global M&A - Indian companies are still displaying growth in the domestic market and are keen on taking on distressed assets abroad. While the global liquidity crisis has ensured that many recent deals have not yet pushed through the pipeline, the number of announced deals has almost doubled in the first half of 2009 proving that Indian firms are still seeking investments abroad. Indian outbound FDI therefore remains a growth market.

Indian companies have an average economic expansion of 8.6% per annum since 2005

India pushes the Frontiers

On the flip side, foreign nations are increasingly welcoming investment from a nation that is prospering during a downturn. According to FDI figures from the UK Department of Trade & Investment, the department managed to secure some 39 successful investments by Indian companies in the financial year 2008-09, a figure that has remained relatively consistent for the past three years. Broken down by sector, Indian firms have invested in businesses operating in the sectors of advanced engineering, life sciences, financial services, ICT and creative industries.

Whereas outbound investment by Western nations has in recent years stagnated as a consequence of the need to concentrate on the domestic ventures, India's outbound growth continued in 2008. According to figures released by Thomson Financial, India made \$24bn of outbound acquisitions 2008, with relative stability expected in 2009 (\$22.5bn projected) in spite of the global credit issues.

India made \$24bn of outbound acquisitions in 2008

India's outward investment figures are bolstered considerably by a small number of deals of significantly high value. In 2007 Tata Steel acquired Corus, an Anglo-Dutch group and Europe's second largest steel manufacturer, for \$12.9bn. This was not the only high profile acquisition for the Tata group, for the following year Tata out-bid investment heavyweight One Private Equity and rival firm Mahindra & Mahindra to buy the Jaguar and Land Rover brands from Ford Motor Company for an estimated \$2.3bn.

Other eye-catching corporate news included metal producer Hindalco Industry's acquisition of Canadian Aluminium manufacturer Novelis for \$6bn, wind energy producer Suzlon's purchase of German energy company Repower, the \$600m acquisition of US-based IT services provider Infocrossing by Wipro and United Spirits takeover of Whyte & Mackay for \$595m. A wide range of sectors illustrating depth and strength of Indian industry.

Foothold in Overseas Markets

In terms of UK-India transactions there have been some notable deals in recent years. According to Corpfin, a part of Experian, there have been a total of 44 acquisitions of Indian companies by UK firms from January 2008 to present. Notable examples include Diageo's purchase of a 15% stake in United Spirits for an estimated \$540m, and HSBC's acquisition of a 93% shareholding in investment management firm IL&FS for approximately \$300m.

Similarly, India has made a number of forays into the UK market of late, including HCL Technologies' \$794m purchase of Axon Group and the \$56m acquisition of Brand Rex, a manufacturer of fibre-optic components by Sterlite technologies. And let's not forget, of course, the Jaguar deal.

UK Trade & Investment supporting investments

Aside from the buyout market, India has begun to appreciate the importance of taking strategic shareholdings in UK companies as a means of gaining a foreign foothold in overseas markets. In 2009 so far Indian companies have embarked on several minority stake acquisitions. Tech Mahindra, an India-based systems integration business has seized the opportunity to acquire a 17% stake in Servista Ltd a London-based provider of outsourced customer care and billing services.

Furthermore, Indian-based Samsara Properties has taken a 4% strategic stake in Orient Express hotels, based in London, for \$13m, and turning to the textile industry, Fabindia Overseas has purchased a 25% interest in EAST Ltd, a London-based Women's fashion retailer.

Realising the Potential

On a more micro scale, some individual regions within the UK are proving particularly attractive to Indian businesses. Since 2005 the North West region has welcomed some 15 Indian firms representing a broad spectrum of industries. In the financial services sector, the State Bank of India and ICICI have opened branches in the region, whereas the Tata Group has made two significant add-on acquisitions in the chemicals sector, with Pearl Group and Brunner Mond.

Aside from M&A, Indian businesses are realising the benefits of establishing a presence in the North West. It is for this reason we have seen telecoms provider Sterlite Technologies open a new branch, plastics manufacturer JJ Poly Impex launch a marketing office and computer services group Palpap establish a knowledge centre - all in the North West region.

Appreciating the role that Indian firms can play in stimulating growth, some regional development agencies are playing a big part in encouraging investment. In the North West region, for instance, the NWDA sourced six FDIs from India into the North West in 2008-9. These investments had a direct impact on employment, creating 120 new jobs and safeguarding 110 further jobs, with the average wage standing at £24,000 per annum.

On the back of these successes, several other UK regional development agencies are looking to open their doors to Indian investment. By means of an example Advantage West Midlands, a UK-based Regional Development Agency has recently appointed Deloitte's Indian team to act as a lead generator for attracting inward investment from India.

Repaying the Compliment

India is, now more than ever, a land of opportunity and one that UK firms are looking towards. India's IT and technology sectors continue to attract UK investment and its services industry continues to grow apace. Accompanying this is a need for a robust infrastructure. UK businesses have supported these developments for many years and continue to do so in spite of the global economic crisis. In return, Indian companies that have grown as a result of the billions of dollars of inward investment, are now turning to the UK to repay the compliment.

Indian GDP Growth

The prospects for Indian GDP growth in 2009-10 are wide ranging:

8% – Dr Pronab Sen, India's Chief Statistician

6.5-6.7% – Prime Minister's Economic Advisory Council

4.5% – International Monetary Fund

4% – The World Bank

6.1-6.5% – The Confederation of Indian Industry

6.5-6.7% – Reserve Bank of India

However, as the ripples of the Western crisis reach India's shores, the country has registered a 6.7% GDP growth, falling short of the government's forecast of 7.1%.

But compared with other big hitters such as the US which experienced a negative GDP growth of 5.7% in Q1 2009* and the UK which is forecast to see a 2.2% contraction in GDP in 2009**, and against the backdrop of projections by the IMF that global that the world economy will contract by 1.3% in 2009, India has a steady foothold in the world economy.

*Source to the Bureau of Economic Analysis

** Source to the British Chambers of Commerce



European Attractiveness Survey

Ernst & Young's 2008 European Attractiveness Survey questioned 834 decision-makers about how they see the attractions of alternative business locations, and the criteria that drive their perceptions.

For the first time, Europe is no longer the most appealing location. The most important driving force for foreign direct investors is to access new markets. And as Europe's economy slows, they are increasingly looking to thriving economies and competitiveness elsewhere.

Today, business leaders see the investment world as multi-polar, with destinations such as China, India, Russia, and the Middle East, which enters the top ten ranking for the first time, now strong rivals to the traditional dominance of Europe and the US.

However, as Europe's long-established inward investment champion, the UK is more resilient than its main Western competition - France, Germany and Spain. The UK is ranked #1 both in terms of the number of FDI projects (713) and also in terms of the number of jobs created as a result of FDI (24,416)



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