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Charting Dynamic Trajectories: Multinational Firms in India

In this article, we provide a synthesizing framework that we call the “dynamic trajectories” framework to study the evolution of multinational firms (MNCs) in host countries over time. We argue that a change in the policy environment in a host country presents a focal MNC with two sets of interrelated decisions. First, the MNC has to decide whether to enter, exit, or stay in the host country at the onset of each policy epoch; second, conditional on the first choice, it has to decide on its local responsiveness strategy at the onset of each policy epoch. India, which experienced two policy shocks—shutting down to MNCs in 1970 and then opening up again in 1991—offers an interesting laboratory to explore the “dynamic trajectories” perspective. We collect and analyze a unique dataset of all entry and exit events for Fortune 50 and FTSE 50 firms (as of 1991) in India in the period from 1858 to 2013 and, additionally, we document detailed case studies of four British and American MNCs (that arguably represent outliers in our sample).
In a report published in November 2012, Computerworld reported that IBM’s India workforce likely exceeded the size of the U.S. IBM workforce. Earlier, in March 2009, IBM was in the news for outsourcing thousands of technology jobs from the United States to India. BusinessWeek reported that the worldwide workforce at IBM went from 386,558 at the end of 2007 to 398,000 at the end of 2008. But U.S. IBM employment fell from 121,000 to 115,000 during the same time. These developments were ironic for a firm that was asked to leave India in 1977 because it refused to comply with local regulations. IBM’s exit from India and subsequent reentry was in stark contrast to the continued presence in India of British multinationals such as Unilever and British American Tobacco (BAT).

In this article, we develop a historical perspective on the policy regime change related to multinationals in India and describe, using both time series and across-home-country variation, the different reactions of multinational firms (MNCs) to the same policy events. We analyze the events through two epochs—India shutting down to MNCs in the 1970s and reopening to MNCs in 1991 (i.e., 1991 onward)—and develop insights into how multinationals chart varied dynamic trajectories during these two epochs. We argue that for a focal MNC, such a change in policy environment represents two sets of decisions. First, the MNC had to decide whether to exit or stay in India in the 1970s and then whether or not to reenter in the 1990s (conditional on exiting in the 1970s). Second, at the onset of each policy epoch, the MNC had to decide on continuity or change in its local responsiveness strategy, represented by investments in the input side (manufacturing plants, plantations, trademarks, patents, and talent), output side (functional focus, product mix, pricing, distribution, etc.), and host country government relationships. We also argue that both the direction (i.e., what lever the MNC uses to change local responsiveness: investment in physical, intellectual, or human capital or modifications in functional focus and product mix) and the degree (i.e., the extent) of change in local responsiveness are endogenous to the decision to stay/exit/enter. As an example, if an MNC decides to stay at the onset of a negative policy epoch, it might decide to focus on changing its local responsiveness strategy on the input side and concentrate less on drastically changing the product or functional mix for reasons of continuity. However, if the MNC follows an exit/reenter strategy, it might be able to drastically alter its functional and product mix on
reentry after several decades, as there are fewer concerns about continuity with the passage of time. Investments in the input side also generate employment—a lever used to navigate difficult government negotiations.

Given these strategic choices to be made at the onset of both policy epochs, MNCs have a choice of decisions, leading to possible dynamic trajectories in the host country. We will detail this “dynamic trajectories” framework later. We also collect and analyze a unique dataset of all entry and exit events for Fortune 50 and FTSE 50 firms in India in the period from 1858 to 2013 and, additionally, we document four detailed case studies of British and American MNCs to develop the dynamic trajectories perspective. The four case studies, developed using archival and other data gathered from multiple sources, such as LinkedIn, arguably represent extremes in our sample. While the two British multinationals, Unilever and BAT, followed a well-crafted “stay/stay” strategy, the two American multinationals, Coca-Cola and IBM, successfully executed an “exit/reenter” strategy. The study of extreme differences in strategy is intended to identify large differences in the adoption of dynamic trajectories. We start the analysis with a description of the policy regime in India prior to 1970.
Indian Policy toward MNCs Prior to 1970

Business historians have long studied the history of multinational firms in India. Tirthankar Roy, in his article in this special issue of the *Business History Review*, provides a history of foreign trading firms in colonial India. He outlines how European trading firms started in Calcutta as agency houses and attracted Scottish, Welsh, English, German, and French capitalists. Some of these firms moved inland and focused on indigo processing factories while the rest remained in Calcutta and conducted three functions related to the indigo trade: shipping, financing, and insurance. After the Indian mutiny ended and Crown rule began in 1858, “born-industrial” foreign firms that had become industrial after a relatively short period in trading entered India. Examples of such firms included Andrew Yule in tea, jute and coal, McLeod Russell in tea, Balmer Lawrie in engineering and coal, Bird Brothers in jute and coal, etc.²

In *Multinationals and Global Capitalism*, Geoffrey Jones documents the evolution of India as a destination of inward foreign direct investment (FDI) over time. In 1914, India was ranked eighth (behind the U.S., Russia, Canada, Argentina, Brazil, South Africa, and Austria-Hungary) in terms of inward FDI. In 1929, India ranked third, only behind Canada and the United States.³ B. R. Tomlinson provides several estimates of FDI in India from 1921 to 1960.⁴ By 2002, according to Jones’s estimates, India had fallen way behind as a destination for inward FDI, with only 0.4 percent of the world total FDI. In his book *Dislodging Multinationals: India’s Strategy in Comparative Perspective*, Dennis Encarnation describes the decline of British colonial agencies and the evolution of Indian business houses and new British multinationals in India over time, starting with Independence in 1947. He outlines “The Indianization of Colonial Enterprises” post-1947.⁵ Given that the London and Liverpool headquarters of these agencies were not able to invest overseas, Indian business houses began to invest capital in the British agencies and, by mid-1948, Indian businesses held more than 85 percent of the equity in colonial managing agencies. The takeover of British business interests in India, particularly in Bengal, was largely engineered by Marwari business groups (including the Birla family, Juggilal Kamalpat, and Surajmull Nagarmull). Tomlinson provides a detailed account of this shift in ownership.⁶ In “The Maturing of Multinational Enterprise: American Business Abroad from 1914 to 1970,” Mira Wilkins documents that U.S. direct investment in India in 1929
was $32.7 million, a mere 0.4 percent of the total U.S. direct investment abroad ($7.55 billion) in 1929.\textsuperscript{7}

Post-independence the institutional environment for multinational firms changed quite rapidly. Matthew Kust writes, “foreign enterprise no longer has its own way as it did when India was under foreign rule.” On April 6, 1949, Indian Prime Minister Jawaharlal Nehru released a policy statement on foreign enterprise in the Constitutional Assembly of India, stating, “As a rule, the major interest in ownership and effective control of an undertaking should be in Indian hands. . . . Government will not object to foreign capital having control of a concern for a limited period if it is found to be in the national interest.” During the first years of independence, foreign enterprise almost never gained majority ownership of a new industry; Kust notes that one “notable exception was the licensing of three oil refineries to Stanvac, Caltex and Burmah-Shell during the early 1950s where 100 percent foreign ownership was granted.”\textsuperscript{8} Majority ownership by foreign enterprise was a rare exception with only 26 of more than four hundred collaboration agreements concluded in 1961 giving the foreign company majority ownership. In addition, in 1955, the Fourth Amendment to the Indian Constitution removed from the scope of judicial review the adequacy of compensation upon state acquisition of private property and business interests. After this amendment, India nationalized the Kolar gold mines, which had been completely British owned, and the Imperial Bank and the life insurance business, which had minority foreign ownership. In his book \textit{Foreign Enterprise in India}, Kust described the policy instruments on industry classification, licensing, capital controls and taxation employed by the government of India to protect “new (domestic) industry.”\textsuperscript{9}

In the years leading to 1970, India’s policy toward multinational firms was captured in a central planning policy document known as the “Five Year Plan.” The first Five Year Plan (1951–1956) outlined that foreign investment was allowed where the nation needed new production lines; where special skills not available locally were required; and where the domestic production volume was insufficient to meet demand and there was no expectation that indigenous industry could expand quickly. In 1961, the government also released a list of industries where foreign investment was particularly welcome, noting the gaps in production capacity of the nation. The list included extremely profitable industries, such as pharmaceuticals, aluminum, and fertilizers. This policy regime attracted several
multinational corporations, particularly pharmaceutical companies, to India. In 1970, in fact, India was home to forty-six foreign pharmaceutical companies. The Hathi Committee of 1975 noted the evolution of pharmaceutical MNCs setting up manufacturing subsidiaries in India. These companies were attracted to India because of its large domestic market, mild drug control measures, limited competition, and tax concessions. The government also sent out invitations to MNCs such as Glaxo, General Motors, and Ford Motor to invest in India, with an informal suggestion to include local equity. MNC investments increased substantially in the 1957–1963 period.

However, foreign firms did face certain constraints in conducting business in India. The Indian currency, the Rupee, was nonconvertible and high tariffs and import licensing prevented foreign goods from reaching the market. Any business that wanted to operate in India needed a license and several permits. Multiple restrictions required companies to go through several government departments before getting permission to set up shop in India: A firm would have to get the green flag from up to eighty agencies before it was granted a license to produce in India. Even after getting a license, the state interfered in matters like the nature of the item produced and the quantity and pricing of the finished product (in certain industries). The state also prevented laying off workers and closing factories as well as limiting the number of licenses it issued in each industry. Each industry had a cap on licenses, usually four or five for the whole nation, creating a monopolistic market. Investors focused on procuring licenses rather than on improving their services and products. Owing to the limited number of players, a license guaranteed profits. Thus, regulation, with extreme controls on FDI, along with a high tariff wall, sheltered domestic companies from overseas competition. This policy emerged from the nation’s socialist viewpoint and the prior experience of colonial exploitation, but this monopolistic situation hurt the country’s overall infrastructure.

1970: India Shuts Down to MNCs

In the early 1970s, the Indian government gradually began tightening the regulatory noose on MNCs operating in the country. This shift was driven by a concerted effort by the Indian state and local firms to “dislodge” multinationals from India. Encarnation outlines a “causal model” of how MNCs were dislodged from India: In the first step, local
firms gained financial independence and managerial autonomy from MNCs; in the second step, Indian firms began to secure technology free of foreign capital; and in the third step, Indian firms acquired control of markets previously dominated by MNCs.\textsuperscript{11}

From a policy point of view, this converged into two new policies designed to control India’s economic resources and foreign interests, especially to curb the outflow of capital in the form of earnings. Both of these policy instruments directly affected multinational firms. We first examine the Foreign Exchange Regulation Act (FERA).

FERA was passed by an act of Parliament in 1973 and came into effect on January 1, 1974. This act consolidated and amended the previous FERA Act of 1947. FERA goal was to restrict dealings in foreign exchange and other securities that could impact the nation’s currency and foreign exchange reserves. The act had a provision to cap the foreign investment in all companies operating in the nation, and foreign companies had to dilute their shareholdings to 40 percent. FERA also vested power in the hands of the Reserve Bank of India (RBI) to regulate the foreign equity in the companies operating in India and to ensure that the cap was maintained. As a result, all companies came under the direct control of the Reserve Bank of India.\textsuperscript{12} All firms operating in India with more than 40 percent foreign equity had to obtain permission from the RBI to continue operations after January 1, 1974. FERA affected already-established foreign companies in India that had foreign equity stakes exceeding 40 percent, and it applied regardless of a firm’s initial terms and conditions. FERA also outlined that all companies operating in India (with the exception of foreign airline, shipping, and banking companies) would be incorporated under the Indian Companies Act, which would curb tax-free outflows of profits. Additionally, the maximum foreign equity percentage stake was differed by industry. Violations of FERA would incur criminal charges.\textsuperscript{13}

Out of the 881 companies that applied to the RBI, only 150 companies were allowed to keep a higher level of foreign equity than the prescribed cap; the others diluted to fit the ambit of FERA. Companies that found the terms unacceptable began to wind up operations in India. Fifty-four companies applied to exit India by 1977–1978 and nine companies applied to exit in 1980–1981.\textsuperscript{14}

In addition to FERA, the Indian government introduced the Patent Act of 1970, and this policy change had far-ranging implications for both multinational and domestic firms, particularly in the pharmaceutical industry. The two policy instruments, FERA and the new patent act, were introduced within a span of three years and represented parallel attempts to tighten control of MNCs. In accordance with Encarnation’s causal model of dislodging MNCs, the new patent act intended to level the playing field for Indian firms in the domain of intellectual property.\textsuperscript{15}

As of 1970, multinational companies controlled 68 percent of the market share in India’s pharmaceuticals. These multinationals—with the support of the Patent Act of 1911—prevented local Indian companies from manufacturing new drugs. The patent law allowed the MNCs a monopolistic position, and they used their stronghold on the market to charge extremely high prices, resulting in little access to medicines for the Indian masses.

The Indian government replaced the Patent Act of 1911 and also decided to introduce drug price controls through the Drug Price Control Order of 1970. The Patent Act of 1970 represented a set of rules that laid out the legal management of intellectual property in India. The act was a keystone in the nation’s treatment of intellectual property.

The central piece of the patent law was that it recognized only process patents and not product patents in the pharmaceutical and agrochemical sectors. It also reduced the patent period from sixteen years to seven years in these sectors and to fourteen years in other cases. This process patent regime triggered reverse engineering in the Indian pharmaceutical sector for drugs patented in other countries. Indian companies could now discover alternate processes for manufacturing drugs that were not patented in India.\textsuperscript{16}

In summary, from 1970 to 1990, FERA and the Indian Patent Act of 1970 had leveled the playing field for Indian firms with regard to MNCs. FERA gave Indian firms financial and managerial autonomy from foreigners and the patent act gave Indian firms an opportunity to reverse engineer products.

1991: India Reopens Doors to MNCs

By the early 1990s, India was deep in an economic crisis triggered by both political and economic factors. The two years prior to 1991 had seen political turmoil, with four
prime ministers and four finance ministers. This led to unclear policies and virtual economic paralysis. The years prior to 1991 saw increased defense expenditures, reduced tax revenue, slow growth in the export market, and a lack of a coherent budget, which brought about an ever-increasing deficit and inflation. FERA was hampering India’s ability to compete with other countries. During the Persian Gulf War, India had purchased oil at an extremely high price, and instability in the Middle East affected India as well. Additional problems included an annual rate of inflation of 17 percent, an unsustainably large fiscal deficit, and widespread flight of capital. The need for economic reform was further accentuated by the collapse of the Soviet Union, a country with which India had had strong political and economic ties.

A major concern in 1991 was the unprecedented possibility that India would default on its external debt, something that had not happened since independence. India’s foreign debt stood at $72 billion, making it the world’s third-largest debtor after Brazil and Mexico. This growth in debt was rapid, as the foreign debt of the nation stood at $20.5 billion in 1980. In 1991, India had only $1.1 billion in its hard currency reserves, enough for only two weeks of imports. Realizing that it did not have enough money to pay for its imports and was nearly bankrupt, India reconsidered its stance on Western influence. The government entered talks with the International Monetary Fund (IMF) to seek emergency aid. India needed more than $5 billion from the IMF to meet its immediate obligations. Taking such a huge loan from the IMF would grant the IMF substantial lobbying power with India, as the international body disbursed loans under “conditions that often included altering policies viewed by the fund as mistaken or counterproductive.” Among the IMF’s demands was a reduction of the budget deficit, a decrease in the licensing requirements for companies, opening doors for foreign companies, and liberalizing investment.

Though India was traditionally socialist in its policies after Independence, this was not the country’s first attempt at economic liberalization. A prior attempt in 1966 was reversed in 1967, after which a stronger socialistic model was adopted. The next major attempt was in 1985, driven by Prime Minister Rajiv Gandhi; it came to an end in 1987. The four or five licensed producers in each industry were instrumental in blocking the 1980s reforms.
Spurred by the IMF in 1991, the government of Prime Minister P. V. Narasimha Rao and Finance Minister Manmohan Singh pushed for structural policy reform. These policies included opening the country to international trade and investment, deregulation, privatization of state-owned entities, tax reforms, and inflation-controlling measures. The country went through a deregulation makeover—one that encouraged foreign investment.

Since 1991, arguably India has sustained the spirit of liberalization, despite changing governments, making these reforms more sustainable. This liberalization resulted in India’s rising GDP growth, peaking at 9 percent in 2007. With the economic reforms came relaxation of the FDI norms. While the GDP growth of the nation prior to 1990 was a little under 4 percent on average, the GDP growth postreform stood at between 6 and 7 percent toward the end of the 1990s.

FERA was repealed in 1999 by the government of Prime Minister Atal Bihari Vajpayee. The less stringent Foreign Exchange Management Act (FEMA) replaced it, loosening restrictions on foreign exchange and investment in India. FEMA was more aligned to the new economic reforms the nation was witnessing. FEMA made all violations regarding foreign exchange civil, not criminal, offenses, making it more investor friendly. FEMA tried to consolidate legislation relating to foreign exchange in India, with an ultimate goal of allowing external trade and payments, and to facilitate the development of a foreign exchange market in India. The reforms also immediately reduced the number of steps required to procure a license to four or five approvals, mainly environmental. Most goods underwent a tariff cut, apart from goods in the consumer sector.

Indian Patent Reform Starting 1999

Following FEMA, the Indian patent system underwent a number of reforms starting in 1999, triggered when India signed the agreement on Trade Related Aspects of Intellectual Property Rights (TRIPs) at the World Trade Organization and joined the Patent Cooperation Treaty (PCT).

Product patents in medicine, food, and agrochemicals were now allowed and the patent expiry period was extended to twenty years, similar to that in the U.S. The average time required to get a patent was reduced from five to three years. The patent filing fee did not change during this period and remained substantially less compared to that of the
United States Patent and Trademark Office (USPTO). The patent system also granted exclusive marketing rights (EMRs) based on patents granted; this enabled multinational firms with patents to derive competitive advantage in selling their patented products. In the past twenty years, Indian patent law has been amended three times—in 1999, 2002, and 2005—to increase compatibility with TRIPs and to allay MNCs’ fears of intellectual property theft.

With the Indian patent reforms, a lot of MNCs’ worries regarding intellectual property protection seemed to disappear. An analysis of Indian patent filings shows a steep rise in the total number of patents filed in India, with an inflexion point in 1997. This increase is attributed to positive expectations about the 1999 reforms. From 1995 to 2004, MNCs from fourteen countries filed a total of 8,426 patents, of which MNCs from the U.S. filed the most (2,477 patents), followed by firms from Germany and Switzerland. Patent applications by foreign MNCs in India started increasing further around 2000 and have been increasing ever since. The EMR, “mailbox” provisions, and the belief that India would abide by TRIPs, gave MNCs confidence, leading to a surge in the number of applications. In contrast, Indian entities filed 1,486 applications in the same period. The number of patents filed in India ranged between 2,000 and 4,000 patents per year from the early 1970s all the way to 1993. Post-1993, there was a rapid increase in the number of patent filings with a spike of around 10,000 patents per year in 1997, in anticipation of the 1999 reforms.

MNCs Stream into India: Analysis of Fortune 50 and FTSE 50 MNCs

With the initiation of economic reforms, India attracted unprecedented foreign direct investment. Average annual FDI rose from $100 million in the mid-1980s to around $2 billion in the mid-1990s. The stock of FDI rose from less than $2 billion in 1991 to almost $39 billion in 2004. The World Investment Report (WIR) of 2007 indicates that the 1990 inward stock level of FDI was roughly $1.7 billion; the 2000 inward stock was $17.5 billion and the 2004 inward stock was $38.7 billion. The city of Bangalore became one of the largest magnets of foreign investment in India; in 2001–2002 alone, a total of 230 MNCs set up offices in Bangalore’s industrial parks, employing 25,000 engineers.
In this section, we analyze unique data that documents every entry and exit event for each Fortune 50 and FTSE 50 multinational firm. The entry and exit events were tracked from 1858 to 2013 and multiple data sources were used, including historical narratives of several firms, SEC company filings (the complete list of subsidiaries was found in Form 10-K, Exhibit 21 for each firm), and data on company registration in India from the Ministry of Corporate Affairs (MCA) and the Government of India. As the Fortune 50 and the FTSE 50 lists have changed over time, we have compiled data for the lists as of 1991 as well as 2013. In our primary analyses, we use the Fortune and FTSE lists from 1991, the year of the IMF-induced reforms; in the Appendix, we report results using the Fortune and FTSE lists from 2013.

There are several limitations in conducting historical analysis using currently available primary data. Mira Wilkins describes these limitations as sometimes introducing “blinders that obscured important past occurrences.” To circumvent some of these constraints, in addition to conducting our own primary research, we based our analyses on prior articles in business history on multinational entry in India. Appendix Table 1 documents the data on the entry and exit of Fortune 50 multinational firms as of 1991 with operations in India over the period 1905–2013. Appendix Table 2 documents the data for the FTSE 50 firms as of 1991 with operations between 1858 and 2013.

Analysis of the data in these tables reveals several interesting insights. In comparison to the FTSE 50, Fortune 50 MNCs exhibit greater number of entries, but also greater numbers of exit events. While Fortune 50 firms have a total of forty-seven entry events, the FTSE 50 firms only have twenty-nine entry events. On the other hand, FTSE 50 firms have a total of four exit events in this period while Fortune 50 firms have a total of twelve exit events. Between 1971 and 1990, Fortune 50 firms have a total of seven exit events while FTSE 50 firms only have one exit event.

In addition, Fortune and FTSE firms had differences in functional focus. Fortune 50 firms had a more balanced focus in terms of manufacturing and sales/services while FTSE 50 firms had a greater focus on sales/services. Also, the Fortune 50 firms show a slightly higher concentration on R&D in India compared to the FTSE 50.
We compare the entry mode of both categories of firms as well as study whether the firms entered solo or otherwise. A non-solo entry refers to an entry through acquisition or a joint venture (JV), whereas a solo entry represents the firm entering by itself.

Business historians have long studied MNCs’ choice of entry model (joint ventures vs. acquisition vs. solo entry). Encarnation also describes the evolution of joint ventures between multinational firms and Indian business houses. From 1948 to 1957, the Indian government prohibited foreign takeovers of existing local firms and proscribed foreign-owned portfolio investments. India averaged fewer than forty new foreign collaborations annually in this period, most of them with Indian business houses such as Tata (which had sixty joint ventures with foreign partners by 1958), Mahindra, and Bangur. The years from 1947 to 1957 also witnessed the takeover of the British colonial managing agencies by the Indian business houses. Encarnation also documents a foreign exchange crisis that affected India in 1957 that led to a reversal of government policy toward JVs. Government regulators began encouraging Indian firms to seek foreign equity, and local enterprises that secured foreign tie-ups also had better chances of securing the licenses needed for expansion. Encarnation indicates that JVs with foreign multinationals started dramatically increasing from 1958 and hit peak levels during 1964. However, JVs with foreign multinationals started declining in the late 1960s and, as a result, stocks of foreign equity invested in the private sector began to shrink and reached their lowest levels in 1973, the year government policy flipped again with the passage of FERA. Our analysis is an attempt to augment this historical narrative.

The Fortune 50 firms exhibited a preference towards solo entry before 1970 (62 percent of entries). However, between 1971 and 1990, 90 percent of the Fortune 50 entries were either a JV or an acquisition. In the 1990s, the Fortune 50 firms increased the percentage of solo entry to 37.5 percent. FTSE 50 firms were more stable, with only a single solo entry between 1971 and 1990 and post-1991; 83 percent of entries were either a JV or an acquisition in both periods.

The Dynamic Trajectories Framework

Our analysis of selected MNCs reveal important distinctions in the trajectories followed by British and American multinational firms over four decades. There are
differences in whether or not they exited India in the 1970s and in how they crafted their local responsiveness strategies both in the 1970s and the 1990s. We now outline a new “dynamic trajectories” framework to show that adopting certain strategic decisions at the onset of different policy epochs leads to path dependencies resulting in different long-term trajectories for the focal firm in the host country. The dynamic trajectories framework is based on the premise of two policy epochs in a host country—one unwelcoming of MNCs (“negative epoch”) and the other welcoming of MNCs (“positive epoch”). A focal host country could experience a negative epoch followed by a positive epoch or vice versa.

We argue that an MNC manager in the host country must make two sets of decisions at the onset of each policy epoch. The first decision is whether or not to be present in the host country during either or both policy epochs. Here we assume that the MNC is present in the host country prior to the start of the first epoch. If the negative epoch is followed by the positive epoch, the manager has to decide whether to exit or stay at the onset of the negative epoch. Also, conditional on exiting in the negative epoch, the manager also has to decide whether or not to reenter at the onset of the positive epoch. We also assume that, conditional on staying at the onset of the negative epoch, the manager decides to stay during the positive epoch. An MNC thus must face three possible choices: exit/reenter; exit/do not reenter; or stay/stay.²⁹

However, if the positive epoch is followed by the negative epoch, the manager has two possible choices: stay/exit; or stay/stay. We assume that the MNC stays during the positive epoch.

The second decision set relates to whether or not the manager of the MNC in the host country modifies the “local responsiveness strategy” of the firm at the onset of each policy epoch and how the manager crafts changes in that strategy. According to business scholars Christopher Bartlett and Sumantra Ghoshal, MNCs have to concurrently manage the following three priorities: global efficiency; national responsiveness; and worldwide learning. A key strategy element of this three-dimensional framework is the importance of each foreign subsidiary in managing the overall MNC strategy. Bartlett and Ghoshal call this strategy element “local responsiveness” or “multinational flexibility” and define a “differentiated and specialized role” for each MNC subsidiary.³⁰
We build on this construct of local responsiveness and argue that the MNC in the host country could craft changes in the local responsiveness strategy by investing in inputs, outputs, and/or host country government relationships. Investments in inputs relate to physical, intellectual, and human capital—e.g., plants, plantations, trademarks, patents, and talent. Crafting changes on the output side could include altering the functional focus of the firm (to focus on distribution, sales, or manufacturing), choosing new businesses enter, changing the product mix for each business, and modifying the local pricing or distribution strategy for each product. Finally, investments in host country government relationships might involve investments in managing government stakeholders and/or crafting negotiation strategies to navigate host country policy interventions.

Figure 2 outlines the “dynamic trajectories” perspective for a host country experiencing a negative policy epoch followed by a positive policy epoch, from the perspective of a multinational that was in the country already at the onset of the first epoch. The horizontal lines in the figure represent the three possible dynamic trajectories. In addition, for options 1 and 3, at the onset of each epoch, the MNC has to decide whether to maintain or modify its local responsiveness strategy. If the MNC decides to maintain its prior local responsiveness strategy, the MNC manager in the host country does not make any significant new investments in the input side; makes no changes to the functional focus and product mix; and makes no changes in managing government stakeholders. Still, if the manager of the MNC in the host country modifies the local responsiveness strategy at the onset of either or both policy epochs, changes could be made on the input side, the output side, or in managing government stakeholders.

**INSERT FIGURE 2 ABOUT HERE**

It is also plausible that both the direction and the degree of change in local responsiveness strategy are endogenous to the decision of exiting/staying/reentering. We define direction of change as whether or not the focal MNC focuses on input, output, or government relationships and degree of change as the extent and nature of change on any of these levers. We also argue that the direction and degree of change depends on the decision to exit/stay/reenter. As an example, in the face of a negative policy epoch followed
by a positive policy epoch, an MNC that decides to follow a stay/stay strategy might not be able to make drastic changes on the output side (e.g., functional focus, product mix) for reasons of continuity and may instead focus on investments in the input side (e.g., human capital, manufacturing plants, plantations.). However, an MNC following an exit/reenter strategy might have fewer concerns regarding continuity given the passage of time and might be able to make drastic changes to the output side. In that case, the MNC might be able to alter the functional and/or product mix in the host country. In addition, the need to focus on host country government relationships, especially in a negative epoch, might imply a focus on input, since it is related to the creation of local jobs, a key lever to engage with government stakeholders.

We now outline four detailed qualitative case studies of these multinational firms to indicate differences in how they reacted to the two policy epochs in India. The four case studies arguably represent extremes in our sample—while the two British multinationals, Unilever and BAT, followed a well-crafted “stay/stay” strategy, the two American multinationals, IBM and Coca-Cola, successfully executed an “exit/reentry” strategy.31

Further, we show that Unilever and BAT adapted to the negative policy epoch (represented by the FERA regulation and 1970 patent law) by continuously investing in the input side—manufacturing plants and human capital. In contrast, IBM and Coca-Cola exited India following the FERA regulations of the 1970s, subsequently returning with drastically different local responsiveness strategies on the output side represented by different functional and product mixes.

Unilever in India

The first products from the Unilever factories were introduced in India as early as 1888 when Lever Brothers’ Sunlight soap bars made in England were shipped to India. Over time, Unilever brought other products to India—Lifebuoy in 1895, vanaspati in 1918, and Dalda in 1937.32 In 1917, Lever Brothers acquired partial interest in two other British soap companies, one of which had an office and depots in India. Declining British between 1918 and 1921 further triggered Lever Brothers’ interest in India as a manufacturing center. Other factors included the growing local Indian production of soap spurred by wartime shortages, and the widespread Swadeshi movement in India, which advocated self-
sufficiency through use of locally made products. In the 1920s, Lever Brothers bought a
site at Sinduria, near Calcutta. Later, Lever Brothers set up Hindustan Vanaspati
Manufacturing Company in 1931. In 1933, a new company called Lever Bros. (India) Ltd.
was incorporated in Bombay. Subsequently, Unilever set up factories to manufacture soap
in Calcutta and Bombay and vegetable ghee just outside Bombay. Lever Brothers formed
one more subsidiary, United Traders Limited, in 1935.³³

These subsidiaries functioned independently until 1956, when they merged to form
Hindustan Lever Limited (HLL), which sold 10 percent of its equity to the public; the share
of public equity was increased to 14 percent in 1965.³⁴ The country’s planned economy at
the time protected local manufacturers, and Unilever flourished. The company, under the
influence of the government, also recruited Indian managers, naming P. L. Tandon
chairman in 1961—the first instance of an Indian heading a multinational (see Jaithirth
Rao’s contribution to this special issue). Hindustan Lever Limited evolved into a consumer
goods company, with Unilever as its major stakeholder. HLL had been in the beverages
industry since 1903 with its brand Red Label tea. HLL acquired major manufacturers of
tea, including Lipton, in 1972, forming Lipton Tea (India) Limited in 1977.

When the Indian economy tightened in the 1970s, HLL chose to stay in India. As
Jones documents, Unilever disliked the tightening of the economy and it feared the loss of
intellectual property, but “Unilever became a master at delaying tactics, using its extensive
contacts and goodwill . . . to modify regulations, and generally bargaining with
governments.”³⁵ The 1970 price controls dented the profitability of HLL. By 1971, the
vanaspati business was unprofitable and HLL decided to withdraw in 1972. However,
HLL’s synthetic detergents were not regulated and remained profitable. From 1972 to
1974, HLL negotiated with the government to shelter itself from price controls. An
agreement was reached that if large manufacturers released a toilet soap product for the
poor at a controlled price, the price control on other soaps would be lifted. Later, in 1975
vanaspati came out of the price control regime and the Dalda brand was reestablished.

With FERA came the need for most companies to bring foreign shareholding down
to 40 percent, which was unacceptable to Unilever. HLL tried to retain 74 percent, the
permitted amount for core or technology companies. After negotiations, foreign entities
were allowed to hold “51 percent of the equity, provided that 60 percent of its turnover was in the core or high technology sectors, and that it exported 10 percent of its production.”

To meet these criteria, HLL increased exports, especially soaps and detergents, to the Soviet Union. Gradually, the company began exporting more until it became India’s second largest private sector exporter by the early 1980s. HLL also tried to argue that manufacturing its soap with nonedible oils was a sophisticated technology, but the government did not agree.

In 1977, the newly elected government mandated that Unilever go down to the specified 40 percent foreign ownership by 1979. With no way out, HLL began delaying and stalling, asking to reduce the shareholding in two stages—the first stage to 51 percent in 1978, which was implemented. With yet another new government taking over in 1980, the second stage was delayed, and in 1981, the government permitted Unilever to maintain majority holding.

In *Dislodging Multinationals*, Encarnation describes Unilever’s financial engineering strategy to overcome the constraints imposed by FERA. To comply with the requirements of “maximum foreign equity,” Unilever issued fresh equity to Indian investors and dispersed this equity sale among many individual shareholders, each with a small holding. “In 1980, for example, more than 89,000 Indians held 47 percent of Hindustan Lever’s stock, while Unilever held the remaining block of shares.” This ensured that Unilever had unchallenged managerial control over its Indian operations.

Around this time, HLL also started making significant investments in a key input—managerial talent. HLL initiated several management development programs and attracted the best students from the premier Indian Institutes of Management. The company continues to be an attractive employer today; AC Nielsen rated it the best employer of choice for business school graduates of the class of 2013. Arguably, the firm’s talent management programs have contributed to the growth of the broader managerial labor market in India. Company alumni have taken more than four hundred CEO positions (including many within Unilever). The company’s name changed in June 2007 from Hindustan Lever Limited to Hindustan Unilever Limited (hereafter HUL for the years following 2007).
To analyze the impact that the firm’s talent development program had on the broader Indian managerial labor market, we collected and analyzed the attrition patterns of 751 HUL alumni who have since been working in senior management positions in other firms in India. The highest fraction of HUL alumni were working at other firms in the fast-moving consumer goods or FMCG industry (27.8 percent). HUL alumni have also moved to telecommunications (17.8 percent), information technology (16 percent), food and beverages (15 percent), pharmaceuticals (6.4 percent), management consulting (4.6 percent), banking (4.2 percent), and retail (4.2 percent).

Through the 1970s and 1980s, Unilever modified its local responsiveness strategy by making significant investments in the input side—predominantly in talent management programs and manufacturing capabilities. It also successfully negotiated with successive Indian governments and modified its product mix based on the prevailing policy environment.

Post-1991, the company went on a merger-and-acquisition spree, merging with Tata Oil Mills Company (TOMCO) in 1993 and forming the equal stake joint venture Lakme Limited with another Tata company, Lakme Unilever Limited, in 1996. In 1998, Lakme Limited sold its brands and divested its 50 percent stake to HLL. HLL also expanded geographically and set up a subsidiary in Nepal, Unilever Nepal Limited (UNL). In early 2000, the government awarded 74 percent equity in Modern Foods to HLL—an instance of the government divesting its equity in state-owned entities. In 2002, HLL acquired the government’s remaining stake in Modern Foods.  

In the second policy epoch, the company again modified its local responsiveness strategy by making significant investments in inputs by acquiring manufacturing plants; it also made additional investments on the output side by acquiring brands such as Lakme and Modern Foods. Through both periods, the organization has remained focused on manufacturing, marketing, and talent management. Sales grew from around Rs. 75 crore in 1991 to around Rs. 1,800 in 2000, showing a compound annual growth rate of close to 40 percent. As of 2013, HUL sells more than thirty-five brands in more than twenty categories in India—“soaps, detergents, shampoos, skin care, toothpastes, deodorants, cosmetics, tea, coffee, packaged foods, ice cream, and water purifiers.” It employs more than 16,000 employees and has annual sales of close to Rs. 25,206 crore. HUL still operates
as a subsidiary of Unilever, which has a 52 percent shareholding. Arguably, HUL is one of the “most local” MNCs operating in India.

British American Tobacco (BAT) in India

American Tobacco Company (ATC) formed in the year 1890 from the merger of several tobacco firms. Looking to expand its geographies, ATC moved out of the U.S. to countries like India and China only to run into competition from British cigarette manufacturers. ATC therefore acquired British firm Odgen Tobacco Co. As a countermeasure, the British players rallied to form the Imperial Tobacco Co. Ltd. ATC and the Imperial Tobacco Company entered into a price war. Both companies took a beating; to resolve matters, they decided to pull out of each other’s domestic markets in 1902. For entry into foreign markets, they collectively formed the British American Tobacco Company (BAT), with ATC owning a majority stake of 67 percent. While initially BAT relied on factories in the U.S. and the U.K. for supplying cigarettes to foreign markets, the company gradually transitioned to manufacturing the cigarettes locally or in nearby nations for all its export markets.

Prior to the formation of BAT, ATC had made its first foray into India, marketing its products through an agency called George Atherton & Co., which was based in Calcutta. ATC had previously set up distribution facilities centered outside of Calcutta, which were strengthened after the formation of BAT to cover all of India. The volume of imported cigarettes doubled from 1901 to 1905. The India operations, which were initially a branch of BAT, were upgraded to a subsidiary called BAT Co. (India), registered in London in 1905.

BAT’s operations in India transitioned from marketing imported cigarettes to manufacturing cigarettes locally and to even processing leaf that was locally grown.

The boycott movement in India acted as an impetus for the company to set up manufacturing operations. In 1910, BAT Co. registered a wholly owned subsidiary in Calcutta, the Imperial Tobacco Co. of India (ITC), which went on to become the main subsidiary for BAT in India. Within a month, ITC had an issued capital of Rs. 3 million and had taken over BAT Co.’s interests not only in India, but in Aden and Burma as well. ITC had the selling and distribution rights for all BAT products in India, which BAT Co.
had previously held. The increasing tariffs on tobacco imports acted as the catalyst for BAT to look to procure leaves locally. BAT Co. therefore set up the Indian Leaf Tobacco Development Co. (ILTD) in 1912 as a subsidiary. That year, the company began building a manufacturing plant in Bangalore to better utilize the southern tobacco-growing region of Guntur, in which ILTD had offices. ILTD grew rapidly, exporting leaf to Britain in the 1920s. Soon the Guntur headquarters shifted to Chirala, with a buying center located close to the railway station. In 1922 a factory for redrying leaves was also established there.\textsuperscript{45} Thus, BAT had three branches in India—the Peninsular Tobacco Company looking after the manufacturing, ITC as its selling wing, and ILTD responsible for local leaf procurement. By 1921, ITC’s issued capital was raised from Rs. 3 million to Rs. 41.6 million; and Peninsular and ILTD were brought under the direct control of ITC. Furthermore, as the company grew, it shifted offices to Virginia House in Calcutta, which was modeled after BAT Co.’s Millbank, U.K., headquarters. During this period, corporate restructuring resulted in all branches except ITC reregistering in the Isle of Man, U.K.\textsuperscript{46}

In the 1920s, ITC boomed, with sales of cigarettes rising from 3.5 billion to 8.8 billion per annum. A wide sales and marketing network was set up, utilizing local along with English salesmen operating out of five depots in India. A distribution network was set up in parallel, with supplies shipped out of the depots. Indian salesmen understood the domestic market. ITC appealed to sellers by promising to take back unsold or old stock, a benefit that local brands were not offering. Over this, ITC also changed credit from unsecured to secured, which greatly benefited wholesalers.

By 1923, ITC’s had factories in Monghyr, Bangalore, and Saharanpur. The Monghyr factory had its own printing facilities as well. Over the years, the company went through multiple restructurings, changing its name to India Tobacco Company Limited in 1970 and then to I.T.C. Limited in 1974. By 1975, the tobacco leaf business came under ILTD, while the all other businesses—including the factories, printing, sales and marketing, hotels, and exports—were under I.T.C. Limited. At the time, BAT had a 60 percent holding in I.T.C. Limited. While I.T.C. Limited owed its origin to BAT, BAT gradually pulled out its own management personnel, who numbered only seven by 1972. This increase in the percentage of Indians in the management of the company helped the
firm establish deep relationships with stakeholders in the Indian government and was a
driver in the firm’s name change. Its name again changed, to ITC Limited, in 2001.

While other MNCs resented FERA’s regulatory requirement for equity dilution,
BAT accepted it. In fact, BAT began diluting its Indian equity rights starting in 1954, taking
it down to 75 percent in 1969, 60 percent in 1974, to the required cap of 40 percent in 1976.
The dilution freed up equity for institutional investors and private Indian investors. Amar
Nayak discusses most MNCs’ attempts to maintain or increase their shareholdings in the
1970s; in contrast, BAT sought local investors, in contrast to MNCs like IBM, General
Motors, and Ford Motors. However, there were some management disputes between BAT
and ITC in the 1990s, leading to an inquiry into whether ITC violated FERA, which led to
arrests of some top executives of ITC. The case was settled in 1997.47

In the pre-FERA years, the government mandated that foreign firms generate
employment, reduce imports through substitutions by local products, increase exports, and
invest in core industries. While some multinationals left India in the 1970s, BAT continued
to invest in manufacturing and negotiated with key government decision makers. ITC
commenced growing and processing tobacco leaves in the country, thus generating large-
scale employment in the farm sector. According to Encarnation, “The company embarked
on this strategy of ‘phased Indianization’ after it had realized, in the late 1960s, that the
government was unlikely to grant majority foreign ownership to a subsidiary in an industry
(tobacco) that remained closely tied to agriculture, required little new technology or large
capital investments, and had miniscule prospects for exports.”48

To further secure the goodwill of the government, ITC invested heavily in corporate
social responsibility initiatives as well. In 1990, ITC began to export agricultural
commodities; in 2000, it commenced its famous e-Choupal initiative. The e-Choupal
model, which supplied computers with internet access to rural areas, helped farmers more
effectively participate in the supply chain process.

As of 2013, the company is one of the leading FMCG companies in India and its
product portfolio comprises food, personal care, cigarettes, branded apparel, education and
stationery products, incense sticks, hotels, paperboard, agribusiness, information
technology, and more.49 It has successfully built and acquired leading brands in the FMCG,
apparel, and hospitality industries.
In summary, the firm responded to the passing of the two policy epochs by making investments in manufacturing plants and farming, by hiring Indian managers, and by investing in government relationships. In the second epoch, the firm also made investments in the output side by creating new brands.

Coca-Cola in India

Business historian Mira Wilkins documents that in the early 1920s, Coca-Cola’s French bottling plant recorded substantial losses and had to be abandoned. This led Coca-Cola to turn to the policy of licensing bottling plants overseas, rather than direct investment. Up until 1977, Coca-Cola employed the same strategy of licensing bottling plants in India and was the leading soft drink brand in India, flourishing under the government of Indira Gandhi. Coca-Cola was the first multinational soft drink brand in India, having entered in 1956. Prior to that, the market was dominated by domestic brands like Limca. In India, Coca-Cola was incorporated as a “branch” of a consumer goods company.50

But the passage of FERA and the Indian Patent Act of 1970 had a negative effect on Coca-Cola. FERA required that Coca-Cola convert its branch into an Indian company that would divest 60 percent of its stake to Indian investors. The company was given two years to achieve this result. The patent act imposed another condition on the company—Coca-Cola would have to share its drink’s secret formula, nicknamed “7X.” Coca-Cola refused to do this so it exited India in 1977.

Coca-Cola’s departure opened the beverage playing field in India. Local companies began to produce their own soft drinks and began vying for the vacuum that Coca-Cola had left behind. The first player was Pure Drinks, which launched Campa-Cola, and by the end of the 1970s, Campa-Cola was the only cola soft drink in the Indian market. Following suit, Parle, a major competitor, launched Thums Up in 1980; it remains a popular drink in India today. Parle dominated the Indian soft drink market after Coca-Cola’s exit, with a 70 percent market share in 1990.

Despite the new regulations, Pepsi, another multinational firm, subsequently tried to enter the Indian market. The first attempt at entry was in May 1985, when PepsiCo partnered with the RPG Group to form Agro Product Export Limited. It planned to import
the cola concentrate and sell soft drinks under the Pepsi brand, while exporting juice concentrate from the state of Punjab. Since the foreign name of Pepsi was to be used and the cola concentrate was being imported, the government rejected the proposal. The second attempt was through promises of investing $15 million in Punjab for the development of agricultural research centers and various processing units. The investment would create jobs and improve the agricultural processing business in Punjab. Weighing the benefits, the government agreed in 1988. PepsiCo entered India as Lehar Pepsi.

Coca-Cola finally returned to India in 1993 after the economic reforms of 1991. By then, Pepsi dominated the market and Coca-Cola was at an initial disadvantage. Coca-Cola went on to invest $1 billion in India from 1993 to 2003.  

Upon reentry, Coca-Cola modified its local responsiveness strategy by making significant investments on the output side and by drastically modifying its product mix. The company acquired popular Indian brands, introduced several of its mainstream global brands in India, and conducted local R&D to come up with new products to cater to Indian consumers. The passage of time between exit and reentry allowed Coca-Cola to significantly modify its product mix and position itself as a diversified beverage company with both global and Indian brands.

When Coca-Cola returned to India in the 1990s, it acquired the local soft drink brands Limca, Thums Up, Maaza, Citra, and Gold Spot from Parle Agro. Coca-Cola then employed different strategies with each of the brands. The company decided to continue to promote Thums Up, Limca, and Maaza. However, the orange-flavored Gold Spot was in direct competition with Fanta, a product in its existing global product portfolio, and Coca-Cola decided to withdraw Gold Spot from the market even though it was popular in the Indian market at the time.

Coca-Cola, Fanta, Sprite, Burn, and Minute Maid are among the company’s popular international brands that have been introduced in India. In some cases, the company has employed local responsiveness in product design and packaging. As an example, Georgia Gold is not sold as a canned product in India in contrast to other locations. India is also one of the few countries where Coca-Cola sells bottled water under the Kinley brand.
Coca-Cola has also conducted local R&D and has created new products for the Indian market. Minute Maid Nimbu Fresh, first launched in South India in January 2010, is an important product launched for India. The drink was developed exclusively for the Indian consumer and competes directly with Pepsi’s Nimbooz. Coca-Cola also developed a nutritional beverage called Vitingo to address the issue of iron deficiency and iron deficiency anemia in India. Vitingo is a low-cost beverage powder containing iron, folic acid, vitamin A, vitamin C, and zinc. In summary, upon reentry Coca-Cola has made investments to the output side (brands) and, in order to do so, has made investments to the input side (R&D).

IBM in India

Prime Minister Nehru facilitated IBM’s entry into India in 1951. The company had a strong run for nearly two decades before it got into a conflict with the government. The company enjoyed a market share of 80 percent in India, and as IBM had control over which products to market to India, the company essentially controlled the development of the computing industry in the country.

IBM would bring old machines to India and refurbish them, then lease them to the government at inflated rates. Vikram Sarabhai, who headed the government Electronics Committee, intervened. IBM defended its practice, stating that it was trying to meet the nation’s policy of gradual growth. However, the Indian government argued that IBM’s prevailing system of lease and maintenance restricted the development of engineering and programming skills for end users. After the Indian central government established the Department of Electronics (DoE), the DoE wanted to control the development of the computer hardware industry and it initiated a parliamentary investigation into the functioning of IBM.

Additionally, IBM got into FERA-related trouble. According to FERA guidelines, given IBM’s industry, the company had to reduce its equity ownership to 26 percent, which the company did not accept. As it did not comply with FERA, IBM was asked to exit India in 1977.

According to Anant Negandhi and Aspy Palia, “total remittable profits, at the time of phasing out its operations in 1977 were approximately $10 million.”52 The performance
of the company in India was not exceptional, and this was partly attributed to assets sold at less than book value and a high rate of effective taxation (80 to 85 percent).

However, IBM did not completely sever its ties with India after departure. In 1980, it secured its first customer after exiting—CMC, which had been set up to maintain IBM’s computers in India. IBM sent a proposal to the DoE to set up a software development and training institute in 1986, while in 1989 it supplied a major system to the Aeronautical Development Agency. IBM had changed its business model and was doing business as an offshore entity with only a few local employees.

IBM reentered the country in 1992 through a joint venture with the Tata Group. Both the Tata Group and IBM Corporation enjoyed an equal stake in the joint venture, which was called Tata Information Systems Ltd. In 1997, IBM Global Services was launched as a separate company that offered a wide spectrum of IT services, including software development, hardware design, and networking services. In parallel, the name of the joint venture was changed from Tata Information Systems Ltd. to Tata IBM Ltd.

While IBM’s initial operations were based in Bangalore, the company expanded and set up the IBM India Research Laboratory in New Delhi. In 1999, Tata divested its stake in IBM and, following approval by the government, IBM India Limited was launched. IBM India Limited was completely owned by IBM Corporation, except for a 1 percent token holding Tata retained. The Tata Group also withdrew from IBM Global Services (in which it had had a 10 percent stake). IBM India Limited was a combination of IBM Global Services and Tata IBM Ltd.

Tata IBM Ltd. was initially responsible for the marketing and support of IBM products in India, while IBM Global Services offered IT services. Estimates are that Tata IBM had $165 million in sales in 1999 and that IBM Global Services had $85 million in sales. The details of the transaction were not made public by mutual agreement between IBM and Tata, and the move was in accordance with IBM’s global strategy of operating through wholly owned subsidiaries. Since then, the company has been expanding across India, with centers in major cities like Gurgaon, Pune, and Pondicherry; it has also been expanding its offerings within the broad domain of software services.

IBM’s recent growth in India has been rapid. The company’s Indian workforce outnumbered its employees in the U.S. While IBM had less than 10,000 employees in India
in 2002, this sharply increased to more than 120,000 employees in 2011. As of 2010, IBM was the second-largest private sector employer in India, falling short of only Tata Consultancy Services. While the Indian workforce was continuously expanding, the U.S. workforce was shrinking, declining from 121,000 in 2007 to 105,000 in 2009. IBM also made significant R&D investments in India focused on the Indian domestic market. By 2012, IBM’s revenue in India was close to $3 billion. IBM also had six delivery centers in India. In 2009, IBM India spearheaded a research project with a focus on analytics to help telecom service providers and e-retailers with customer acquisitions and service. The project involved scientists in the IBM Research Labs in India and Israel who examined customer trends. IBM Research India is the pioneer in the social network analysis for the company.

Local firms Infosys and TCS pioneered the Indian software delivery model and it can be argued that IBM was borrowing their model when it set up its global services in 1997. IBM bought PricewaterhouseCooper’s global consultancy business and paid $30.8 million for the Indian arm of the company. It also courted twelve of the thirteen individual shareholders of the consulting practice of PwC India, converting them to IBM India employees.56

IBM significantly modified its focus on the output side by changing both its product mix and functional focus. While IBM prior to 1977 was focused on hardware and government sales, post-1991 the firm made a drastic change by abandoning its focus on hardware and by establishing a strong presence in the services and offshore software delivery model. To do this, IBM made investments in the input side by acquiring R&D resources and talent from entities such as PwC.

Conclusion

Over the past several decades, a rich literature has emerged on multinational firms and their relationships with host countries. On the one hand, scholars such as Raymond Vernon and Richard Caves describe a conflict-prone relationship between the host country and the MNC. On the other hand, Richard J. Barnet and Ronald E. Müller depict cooperation and dependency between the host country and the multinational firm. Christopher A. Bartlett and Sumantra Ghoshal outline theoretical approaches as to how
MNCs should balance between the twin priorities of global integration and local responsiveness in the countries to which they expand. In the context of India, Encarnation offers a causal model and empirical evidence of how MNCs were dislodged by the state and local firms.\textsuperscript{57}

In this paper, we develop the “dynamic trajectories” framework to describe how MNC strategy evolves over time to different policy epochs in a focal host country. For a host country transitioning from a negative policy environment toward MNCs to a positive environment (or vice versa), the dynamic trajectories perspective is hinged on at least two sets of salient and inter-related decisions that MNCs have to make at the onset of each policy epoch: (1) whether to stay, exit, or enter the host country; and (2) whether to embrace continuity or change with regard to a local responsiveness strategy. Our model of dynamic trajectories is related to the dynamic capabilities framework in the strategy literature (Teece, Pisano and Shuen, 1991). This framework analyzes the sources and methods of wealth creation, and capture, by private enterprise firms operating in environments of rapid technological change. The dynamic capabilities framework builds on distinctive processes (ways of coordinating and combining), shaped by the firm’s asset positions and the evolution path(s) it has adopted or inherited. The authors also state that the importance of path dependencies is amplified where conditions of increasing returns exist. However, this framework does not explicitly study the evolution of MNC strategy in host countries over time.

We collected unique primary data of entry/exit by Fortune 50 and FTSE 50 firms in India and augmented the same using existing historical narratives of multinationals in India. Using this combination of primary data and existing historical narratives, we develop four in-depth case studies of firms with stark differences in dynamic trajectories to outline how British and American multinationals differed in how they reacted to changes in the policy regime in India.\textsuperscript{58}

As India shut down to MNCs in the 1970s and opened up to MNCs in 1991, American MNCs such as IBM and Coca-Cola followed an exit/reenter strategy. In contrast, British multinationals such as Unilever and BAT followed a stay/stay strategy. There were also important differences in how the MNCs altered their local responsiveness strategy over time. As outlined in the case studies, in the face of a negative policy environment,
Unilever and BAT made investments in the input side (manufacturing plants, human capital, brands) and followed a negotiate/buy time strategy to deal with hostile policy makers. Unilever and BAT also sustained their functional focus on manufacturing. In contrast, IBM started with a sales-only model and a focus on hardware prior to exiting; upon reentry, though, it altered its functional focus and emphasized R&D and service delivery. It also embraced software services instead of hardware as its product mix focus. Coca-Cola had concerns about intellectual property theft at the time of exit; upon reentry, given the new patent regime, it introduced its leading global brands in India and additionally conducted local R&D and created new local brands to cater to the Indian consumer.

Our theoretical model has limitations. The model places disproportionate weight on the two specific episodes of policy in driving decisions by multinational firms in entering a host country and, as an example, does not focus on entry decisions at the onset of the negative policy shock. In the case of India, between 1981 and 1990, eleven US firms entered the Indian economy compared to one firm from the UK. Not only is this the main point of divergence in the historical patterns of British and American firms’ investment decisions (which otherwise track each other quite closely) but it is also a feature that the Dynamic Trajectories framework does not study in detail.

In this paper, we have attempted to provide only a broad outline of the dynamic trajectories framework; much future work is needed to further develop this perspective. For instance, it is not clear *ex ante* whether exiting or staying (in the face of a negative policy regime) and entering or not (in the face of a positive policy regime) is optimal for a focal MNC facing rapid policy change in a host country. For example, for a host country transitioning from a negative to a positive policy environment, a stay/stay strategy could be better in developing host country relationships and in securing concessions from the host government in the long run; however, an exit/reentry strategy could help employ scarce firm resources on the most profitable opportunities anywhere in the firm. Future work needs to develop this analysis both from the perspective of the MNC shareholder and the perspective of the host country stakeholder. There is opportunity for future research to study the performance implications of the exit/reenter strategy compared to the stay/stay
strategy from both the view of the internal shareholder and from the view of the host country stakeholder.

Future research also has an opportunity to “unpack” the antecedents of what drives different MNCs to follow these different dynamic trajectories. For instance, we need to study whether the apparent correlation between these decisions and the home country nationality of the firm is a correlation endogenous to other firm/managerial-level variables or whether there is a deeper causal story related to the home country of the MNC and/or historical ties between the home country and host country.

This paper makes a contribution to the theoretical literature in business history and international business by providing a synthesizing framework that takes into account the element of time and how MNC trajectories in host countries evolve over time. The element of time has been long considered in prior work by business historians describing the evolution of the multinational firm. In The Maturing of Multinational Enterprise: American Business Abroad from 1914–1970, Wilkins (1974) describes “three stages” of multinational growth in host countries. In the first stage (“initial monocentric relationship”), new and distinct foreign units are established or acquired by the parent company “radiating from the parent company.” In stage two, the foreign units develop their “own separate histories” and take on larger functions, introducing new products and sometime acquiring other firms. Over time, the initial monocentric structure is replaced with a “polycentric industrial relationship with heterogeneous foreign centers having varied trading, administrative, and corporate relationships” with the parent. In the third stage, foreign subsidiaries of the multinational firm raise money from where available, often have foreign shareholders, recruit managerial talent in various nations and trade among themselves, often ignoring the parent in constructing intersubsidiary trade deals. To quote Wilkins, “the simple polycentric industrial structure is shattered” and restructuring happens on a “worldwide basis related to product, geographic area, a combination of both.”

Wilkins also writes extensively on how the evolution of the American multinational firm has been influenced by events external to their own operations (e.g., the two World Wars, the Spanish Civil War, the Korean War, the Vietnam War, etc.) and by American foreign policy. From the perspective of host countries, Wilkins writes, “nationalism,
socialism, and communism have had profound impact on the path taken by U.S. international businesses.”  These statements implicitly document that the “path” charted by multinational firms in host countries is influenced by events in the host country, home country, and beyond. In this paper, we attempt to formalize this path dependency of multinational firm evolution in the host country by presenting a synthesizing framework that we call “dynamic trajectories.”

In *Multinationals and Global Capitalism*, Geoffrey Jones (2005) states that the multinational investment in a host country does not always lead to long term benefits for the host country. To quote Jones, “since the nineteenth century, they (multinationals) have transferred resources between countries…however, there have been strict limits to the transforming power of multinationals…the knowledge transfers arising from the huge FDI in developing countries during the first global economy were limited by the enclavist nature of many investments, and by the reluctance to train local workforces.”  In *Multinational Enterprises and the Global Economy*, Dunning and Lundan provide a four-part framework of multinational investment in a host country. Implicit in this framework is the passage of time. In the first phase, the MNC engages in exports and foreign sourcing; in the second phase, the MNC makes investments in marketing and distribution; in the third phase, the MNC initiates “foreign production of intermediate goods and services;” in the fourth phase, the MNC “deepens” and “widens” this value added network; and in the fifth and final phase, this leads to the creation of the “integrated network multinational.”

In summary, though business historians and international business scholars have long considered the element of time in the analysis of MNCs in host countries, we provide a synthesizing framework that captures several of the assumptions that have been more implicit in the literature. Our historical analysis of British and American MNCs in India provides evidence to the existence of different dynamic trajectories followed by MNCs in response to changes in the host country policy environment, and future work will have to explore performance implications of following different trajectories.
1 http://www.computerworld.com/s/article/9234101/In_a_symbolic_shift_IBM_s_India_workforce
likely exceeds U.S.; Web site accessed on 26 July 2013.


5 Dennis Encarnation, *Dislodging Multinationals: India’s Strategy in Comparative Perspective* (Ithaca, N.Y., 1989), [PAGES FOR CH. 2]


11 Encarnation, *Dislodging Multinationals*.


14 Nayak, *Multinationals in India*.

15 Encarnation, *Dislodging Multinationals*.

16 Kumar, *Multinational Enterprises and Industrial Organization*.


21 Analysis conducted by researchers.

22 Information from Technology Information, Forecasting and Assessment Council (TIFAC).


An entry in our sample indicates opening of the Indian subsidiary with a well-defined mandate to sell, manufacture, conduct R&D, etc. An ‘exit’ in our sample indicates closing down of the Indian subsidiary and/or a visible shutting down of all operations in India. Coding was done by two independent research analysts and validation was done by the authors in case of disagreement between the analysts.

Pure R&D entry referring to an entry with the only function of the firm as R&D in India.

Encarnation, *Dislodging Multinationals*, 60.

Theoretically, a fourth option of stay/exit is also possible since latter exit might be motivated by activities in another geography.


40 http://knowledge.wharton.upenn.edu/india/article.cfm?articleid=4536; Web site accessed on 26 July 2013; Rs. 1 crore is approximately $0.17 million using the exchange rate as of July 24, 2013.


45 Cox, “The Global Cigarette.”

46 Ibid.

47 Nayak, Multinationals in India.

48 Encarnation, Dislodging Multinationals, 69–70.


58 Our focus on contrasting British and American multinationals in India is in the spirit of prior work by business historians in the context of India. Mira Wilkins (1974) provides an interesting narrative of how British and American multinationals had conflicting strategies in India in the late 1920s. In 1929, American & Foreign Power acquired a 50 percent stake in the Tata Hydroelectric Agencies Ltd. of Bombay and tried to make an investment in the Calcutta Electric Supply Corporation, “a move that was blocked by British opposition,” (Wilkins, 1974, page 134). In 1947, following India’s independence and following pressure from the Indian government, “American & Foreign Power Company relinquished control of its Indian properties” (Wilkins 1974, page 302).
62 Dunning and Lundan, *Multinational Enterprises and the Global Economy*