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→ Investment Destination Germany: Chances & Challenges for Indian Firms

Not many industrialized nations weathered out the recent global financial crisis as well as Germany has managed to do. The largest economy in Europe has proved to be an agile and versatile player that can boast of a strong domestic base and privileged access to competitive global markets. Supplemented by its excellent physical infrastructure and outstanding technological capabilities Germany offers attractive opportunities for foreign direct investments (FDI). Many Indian firms, buoyed by the increasing Indo-German cooperation, have made use of these opportunities. However, despite increasing engagement there is still room for realizing potential, yet untapped, by Indian firms in Germany.

The German economy registered an early recovery from the recent global financial crisis, growing by an impressive 3.6% in 2010. The fundamentals of the largest European economy consisting of a gross domestic product (GDP) of nearly EUR 2.5 trillion and 82 million inhabitants remain strong even though the pace of growth is expected to slow down to some extent in near future.

Germany has been able to quickly adapt itself to the chances and challenges of a globalized world. In the post-reunification period, its GDP has grown from EUR 1,534.6 billion in 1991 to EUR 2,498.8 billion in 2010, according to the Federal Statistical Office. In the same period its exports have grown from EUR 340.4 billion to EUR 959.5 billion. No wonder, this powerful combination of a strong domestic base and successful foreign trade with the “made in Germany” brand has kept attracting many foreign investors to Germany. In fact, a recent worldwide survey (May 2011) by consultancy firm Ernst & Young has found Germany to be the most attractive FDI location within Europe.

As a consequence of such developments, a growing number of firms from economically emerging countries, such as the BRIC nations, have started discovering Germany as a destination of choice for their FDI. Indian firms buoyed by sustained economic growth of the previous years have been at the forefront of emerging market investors in Germany with close to 200 subsidiaries and over 23,000 employees on their payrolls.

There are several reasons for Indian firms’ overseas expansion. Exposure to global competition has forced firms to seek world-class technological and managerial capabilities. At the same time, domestic and overseas success has put significant slack resources at their disposal. To give an example, the cumulated total profit of Indian firms has increased more than 10-fold between fiscal years 2000/01 and 2007/08, from USD 7.3 billion to USD 74 billion, according to an Annual Survey of Industries, released last year. Encouraged by government support to outward FDI Indian firms have rapidly emerged as a significant source of FDI. Between March 2001 and Sept. 2010 India’s outward FDI stock has increased more than 34-fold, from USD 2.6 billion to USD 89.2 billion according to official data.

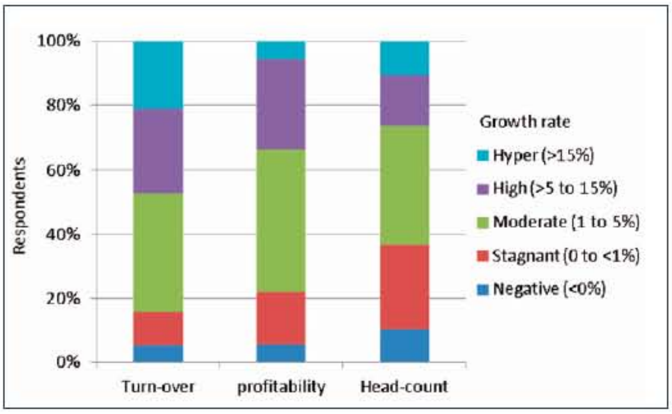
In a significant contrast to their Chinese counterparts Indian firms have so far tended to prefer developed Western countries for their investments. Germany, along with the USA and UK has emerged as a primary target for Indian FDI. The largest economy in Europe provides not only attractive market opportunities. With its established technological prowess, high-quality infrastructure and reliable institutional set-up, Germany is regarded as an excellent investment target by many Indian firms in their pursuit of newest technologies and commercially viable cutting-edge innovations. The two countries enjoy increasingly cordial bilateral relations as witnessed by the regular holding of “India Weeks” in cities like Stuttgart, Cologne and Hamburg.

Indian FDI in Germany

Since many Indian companies prefer to channelize their FDI projects to Germany through their existing domestic subsidiaries or through their daughter concerns in other European countries, the official data fail to capture the true extent of Indian engagement in Germany. The present stock of Indian FDI in Germany, after factoring-in such “indirect” FDI channels, is estimated at about EUR 4.2 billion. Even though recent years have not seen many “big-ticket” investments coming to Germany, there have been several instances of medium-sized FDI projects, such as by Apollo Tyres, Motherson Sumi, the Essar Group, and Kiri Dyes and Chemicals. Also, wind turbine manufacturer Suzlon has continued to intensify its engagement with Hamburg-based REpower Systems. The largest group of Indian firms in Germany (49%) comprises of firms broadly categorized as information technology (IT) firms offering software & engineering services. Other important groups include Automobile & Parts (13%), Manufacturing (11%), and Pharma & Biotech (11%). Indian investments are generally concentrated in the federal states of Hessen, North Rhein-Westphalia (NRW), Baden-Württemberg, Bavaria, and Hamburg. Federal states located in Eastern Germany have so far received less than their fair share of attention by Indian investors even though they generally offer excellent opportunities in terms of infrastructure, financial incentives, and political and administrative support.

Indian Firms in Germany tend to evaluate their performance positively. In a survey conducted by this author at the Hamburg University of Technology, nearly two-thirds of the respondents reported their German operations to be successful. Survey participants were asked about average growth in turnover, profitability and head-count in previous 3 business years. Most firms reported moderate to high success. Whereas 2 survey participants reported high or hyper success on all counts, none had a negative or zero growth for all indicators. However the growth in turn-over did not necessarily lead to higher profitability and or higher headcount.

Figure 3: Average firm growth for 3 key indicators in past 3 fiscal years



In few instances firms reported post-acquisition difficulties such as lower turn-over, increased attrition, extended recruitment time, or reduced quality perception by customers. The silver lining on the wall, however, was that these developments did not seem to be systematic to all Indian acquisitions. Especially firms with a longer presence in Germany or having a higher degree of local management were less likely to face such difficulties. Post-acquisition success therefore seems to correlate with managerial actions and image perceptions in the market.

A comparative analysis showed that firms were more successful when they could muster organizational capabilities to overcome regulatory and bureaucratic hurdles and find a right mix of strategic and operational autonomy. Companies that competed solely on the basis of lower price were found to be on a disadvantage vis-á-vis firms that had an enhanced focus on superior quality and image. Successful firms were more often able to attract and retain local talent. Finally, the ability to bridge cross-cultural gaps in the working styles of the headquarters and the German subsidiary played an important role in success.

Utilizing Unrealized Potentials

Considering the generally positive experience of the Indian firms already present in Germany, one gains the impression that Indian investments of late have struggled to keep pace with the rapidly growing economic ties between the two countries. As demonstrated earlier, Germany with its strong and affluent consumer base, outstanding export credentials, and proven technological prowess could be an ideal partner for Indian firms and entrepreneurs looking to expand their businesses and tap into new markets.

In my opinion, Indian firms would be well advised to take advantage of Germany's excellent physical infrastructure and technological know-how, including in the eastern part, while combining it with their own strengths in production, marketing, low-cost engineering, and business model innovations. Complementary capabilities of the two countries, for instance, could be utilized by Indian firms to develop world-class "frugal innovations" with characteristics that are environment friendly and relatively price worthy. Such innovative products would be ideally destined for competitive global markets apart from the two local markets.

Summarizing, we can say that Germany offers attractive investment opportunities for Indian firms even as the economic ties between the two countries intensify. Many Indian firms have already realized the chances. Still there is a lack of awareness about the chances and challenges present in Germany. Even though Germany is certainly not a cakewalk for Indian investments owing to geographical, cultural and linguistic distances, it is thoroughly possible to achieve success with careful analysis of the market conditions, identification of synergies, and with suitable management practices.

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