



# An Empirical Study On Foreign Institutional Investment FII With Reference To The Indian Stock Market For Future Investment

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## **Abstract**

Foreign institutional investors (FIIs) will shortly be able to purchase shares in India. These days, this is one of the main ways that foreigners use their overseas portfolios to invest in India. To purchase and sell stocks, remit and repatriate cash, foreign exchange investors (FIIs) are required by the Foreign Exchange Regulation Act (FERA) to register with SEBI, obtain authorization from the Reserve Bank of India, and open bank accounts in foreign currencies and rupees. Examining the expanding trends of foreign institutional investment (FII) in India is the aim of the current study. A study has examined the relationship between the returns of the FII and the NIFTY 50 Index. The study with reference to the daily closing prices or another index may provide different sets of results. Also the regression only indicates the dependent and independent relationship and does not guarantee the causation effect. Based on the findings, various investors can learn the behaviour of the relationship and impact of FII with the index returns which can further be used to earn above average returns for Future Investment.

**Key Words:** - Stock Market, FII, SEBI , Foreign Exchange

## **Introduction**

In the modern scenario, the economic growth and development of a country are influenced by many global factors in addition to the domestic ones. This is due to the integration of an economy globally. In general, developed economies of a financial system are stronger than the developing or emerging economies. It is because of the well establishment of a financial system which plays a crucial role in the economic growth of a country. Thus, the financial system is the most important institutional and functional vehicle for economic transformation. Study of Foreign Institutional Investment (FII) in the context of the Indian stock market

involves analysing the impact, trends, regulations, and factors influencing the participation of foreign institutional investors in India's financial markets.

Constituents of Financial System There are three main constituents of a financial **system**:

- i) Financial Assets
- ii) Financial Markets
- iii) Financial Institutions.

### **Objectives of the study:-**

The following objectives of the study are

1. To study the trends of Foreign Institutional Investments (FIIs) activities in the Indian stock market.
2. To study the relationship between FIIs investment and the Stock Market returns in India.
3. To study the impact of FIIs on BSE Sensex, NSE Nifty and also selected sector wise market returns.
4. To study the Foreign Institutional Investors (FIIs) shareholding pattern in the selected companies of NSE.

### **Need for the study**

The reforms in India made a lot of changes in the structure and performance of different sectors in the Indian financial system, in these, stock market becomes part of the reforms. The Indian stock markets performed greatly after the initiation of reforms and Indian stock market become the best destination to the foreign investors. India opened doors to Foreign Institutional Investors (FIIs) to trade in Indian stock market in the form of equity investment with suitable restrictions.

### **Review of Literature from the study**

**Chakrabarti (2001)**, investigated in the paper FII flows to India: nature and cause and found that FII flows are mainly correlated with the equity market returns in India during the study period May 1993 to December 1999, FII flows are more effective than the cause of these returns. **Miles (2002)** attempted to examine the financial regulation and volatility in the emerging equity markets using monthly data on the stock basis for 17 countries over a period ranging from December 1975 to April 2001. This study observed that in Asia, Latin America and other developing countries were opening up, since past decade of the study. Consequently, emerging equity markets were likely to lead to potential benefits in terms of increased financial integration with rest of the world. **Batra (2003)** made an attempt to develop an understanding of the dynamics of the trading behaviour of FIIs and returns in the Indian equity market by analysing daily and monthly data. The study showed a strong evidence of changing trends and adopting positive feedback trading strategies at the aggregate level on a daily basis. However, no evidence of positive feedback trading on a monthly established. **Mishra et al. (2010)** endeavoured to test the causality between FIIs investment

and real economic growth in India over the period 1993 to 2009. The Granger Causality test in the Vector Auto-Regressive (VAR) framework provided the evidence of bidirectional causality running between these two variables. **Yihong Deng and Yongxing Xu (2011)** examine the institutional investors have superior stock selection than individual investors in China by using the data regarding shareholdings of both institutional and individual investors. **Mohanamani.pet al.(2013)** examined the impact of Foreign Institutional Investors on the Indian capital Market. FIIs assured the India's economic growth, which results in corporate earnings continuously in India. **Virender Kumar, Vijender Kumar, Raj Kumar (2014)** have studied the impact of interest rate differentials on net foreign institutional investments in India with data of monthly data from the period April, 2005 to December, 2007 using time series econometric modelling such as Augmented Dickey-Fuller (ADF) test, Granger Causality test which is useful for testing of short-term relationship between variables and Johansen Co-integration test for long-term relationship between variables.

### **Historical Context of FII in the Indian Stock Market**

FIIs were net buyers for five straight years since they were allowed to invest in Indian stock markets in 1992. Since then, the amount of FIIs inflows only grew in numbers. Rs. 79,709 crores in 2013-14, Rs. 1, 11,333 crores in 2014-15, and Rs. 1,19,036 in 2017-18 were some of the years when FIIs bought aggressively.

However, whenever there's a big crisis on the world forum, FIIs tend to rush out of Indian markets. Examples of this are the 1998-99 Asian currency crisis and the Lehman Brothers crisis in 2008-09. During the Lehman crisis, FIIs were the real culprits behind making things look ugly for the Indian stock market as they pulled out Rs. 47,706 crores from India.

### **Overview of Regulations Governing FII in India**

Foreign Institutional Investment (FII) Foreign Institutional Investors (FII) means an institution established or incorporated outside India which proposes to make an investment in securities in India. They are registered as FIIs in accordance with Section 2 (f) of the SEBI (FII) Regulations 1995. FIIs are allowed to subscribe to new securities or trade in already issued securities. Foreign Institutional investors (FIIs) are entities established or incorporated outside India and make proposals for investments in India. These investment proposals by the FIIs are made on behalf of sub-accounts, which may include foreign corporates, individuals, funds etc. In order to act as a banker to the FIIs, the RBI has designated banks that are authorized to deal with them. The biggest source through which FIIs invest is the issuance of Participatory Notes (P-Notes), which are also known as Offshore Derivatives. FIIs are in the form of portfolio investments both in the primary and secondary capital market. They help in bridging the short to medium—term savings-investment gap. FII flows help capital formation either by subscribing to quality issues in the primary market or by releasing the existing pool of risk capital through the secondary market.

## Analysis of FII Inflows and Outflows Over the Years

Foreign Institutional Investors (FIIs) play a crucial role in the stock markets of various countries by investing significant amounts of capital. Analysing the trends in FII inflows and outflows over the years provides insights into the global and domestic economic conditions, investor sentiment, and the attractiveness of a particular market.

Here's a general analysis framework:

- 1. Economic Conditions:** FII investments are often influenced by the economic conditions of the investing and receiving countries. Robust economic growth, stable inflation, and favourable interest rates in the receiving country tend to attract more FII inflows.
- 2. Global Factors:** Global economic conditions, geopolitical events, and monetary policy changes in major economies impact FII flows. For example, during periods of global uncertainty or economic downturns, FIIs may withdraw funds from emerging markets, including the stock market.
- 3. Market Performance:** Positive or negative trends in the stock market can influence FII behaviour. Strong market performance often attracts FIIs, while periods of volatility or decline may lead to outflows.
- 4. Interest Rates:** Changes in interest rates can affect FII inflows. Higher interest rates in the receiving country might attract FIIs seeking better returns, while lower rates may result in outflows.
- 5. Currency Movements:** Exchange rate fluctuations can impact FII returns. Currency depreciation in the receiving country may offset gains for foreign investors, leading to a reduction in FII inflows or even outflows.
- 5. Government Policies:** Policies related to foreign investment, taxation, and market regulations can influence FII decisions. Investor-friendly policies tend to attract more foreign capital.
- 6. Sectorial Trends:** FIIs may show preferences for specific sectors based on global and domestic trends. Monitoring which sectors receive more FII attention can provide insights into changing investor sentiments.
- 7. Political Stability:** Political stability is a critical factor. Countries with stable political environments are perceived as safer for long-term investments, attracting more FII inflows.
- 8. Market Valuations:** Valuation metrics, such as price-to-earnings ratios, can impact FII decisions. Attractive valuations may lead to increased investments, while overvaluation may result in outflows.
- 9. Regulatory Changes:** Any changes in regulations related to foreign investment, market access, or tax structures can influence FII behaviour.

## The Impact of Foreign Institutional Investors (FIIs)

The impact of Foreign Institutional Investors (FIIs) inflows and outflows on the Indian stock market can be significant, influencing various aspects of market dynamics.

**Market Liquidity** FII participation often contributes to increased liquidity in the market. Their large-scale transactions can lead to higher trading volumes, making it easier for investors to buy or sell shares.

**Stock Prices** FII activities can influence stock prices. Increased FII inflows are generally associated with rising stock prices, while outflows may lead to declines. Their investment decisions often reflect confidence in the Indian economy and market prospects .

**Sector Impact:** FIIs may show preferences for specific sectors based on global trends, economic conditions, and growth prospects. Their investments in particular sectors can influence stock prices within those industries.

**Currency Movement** FII transactions involve currency conversions, impacting the exchange rate. Large FII inflows may contribute to the appreciation of the Indian Rupee, while outflows may lead to depreciation.

**Market Sentiment** FII activities can shape market sentiment. Positive FII inflows are often seen as a vote of confidence in the Indian market, boosting investor confidence. On the other hand, sudden outflows can trigger negative sentiments and contribute to market volatility.

**Interest Rates** FII inflows may be influenced by interest rate differentials between India and other countries. Higher interest rates in India relative to other economies can attract FIIs seeking better returns, affecting both equity and debt markets.

**Economic Growth:** FII investments are often linked to the economic growth of the host country. Robust economic performance can attract more FII inflows, supporting the overall health of the stock market.

**Policy Reactions:** Governments and regulatory authorities may respond to FII activities by implementing policies to either encourage or regulate foreign investments. Changes in policies can impact FII decisions and subsequently affect the stock market.

**Volatility and Risk** The presence of FIIs can contribute to market volatility, especially during periods of uncertainty or global economic challenges. Rapid FII outflows can lead to increased market risk.

**Market Integration:** FIIs contribute to the integration of the Indian stock market with global markets. Movements in global markets and changes in international economic conditions can quickly transmit to the Indian market through FII activities.

## Comparison of FII Trends in India with other Emerging Markets.

However, I can provide a general comparison of Foreign Institutional Investment (FII) trends in India with other emerging markets based on historical patterns and factors that typically influence FIIs.

- Market Size and Potential:** India has one of the largest and fastest-growing economies among emerging markets, making it an attractive destination for foreign investors. Other emerging markets, such as Brazil, Russia, China, and South Africa, also have sizable economies and draw foreign investment.
- Regulatory Environment:** The regulatory environment in India plays a crucial role. Changes in policies related to taxation, repatriation of funds, and overall investment climate can impact FII trends. Other emerging markets have their regulatory frameworks, and investor sentiment is influenced by how transparent and stable these regulations are.
- Economic Indicators:** Factors like GDP growth, inflation rates, and fiscal policies influence investor decisions. Stable economic indicators are generally favourable for foreign investment. Investors compare these indicators across different emerging markets to identify opportunities and risks.
- Political Stability:** Political stability is a key factor influencing FII trends. Investors prefer markets with stable governments and policies. Political events or uncertainties can lead to fluctuations in FII flows, not only in India but also in other emerging markets.
- Global Economic Conditions:** FII trends are influenced by global economic conditions. Factors such as interest rates, global trade tensions, and economic crises can affect investment decisions. Correlations between the economic conditions of different emerging markets can be observed, with investors adjusting their portfolios accordingly.
- Sectorial Opportunities:** Investors often assess specific sectors within emerging markets. The performance and growth potential of sectors like technology, healthcare, and finance can attract or divert FII flows. Comparative analysis of sectoral opportunities in India and other emerging markets is crucial for understanding investment patterns.
- Currency Exchange Rates:** Exchange rate fluctuations impact the returns for foreign investors. Stable currencies and favourable exchange rates contribute to investor confidence. Investors compare the stability and potential appreciation of currencies in different emerging markets.
- Global Risk Sentiment:** Events like geopolitical tensions, global economic slowdowns, or health crises (as witnessed with the COVID-19 pandemic) can impact global risk sentiment, affecting FII flows in all emerging markets. It's essential to note that FII trends are dynamic, and various factors can influence investor decisions. Regular monitoring of economic indicators, policy changes, and global events is crucial for understanding the evolving landscape of FII in India and other emerging

markets. To get the most current and accurate information, it's recommended to refer to the latest reports from financial institutions and market analysts'

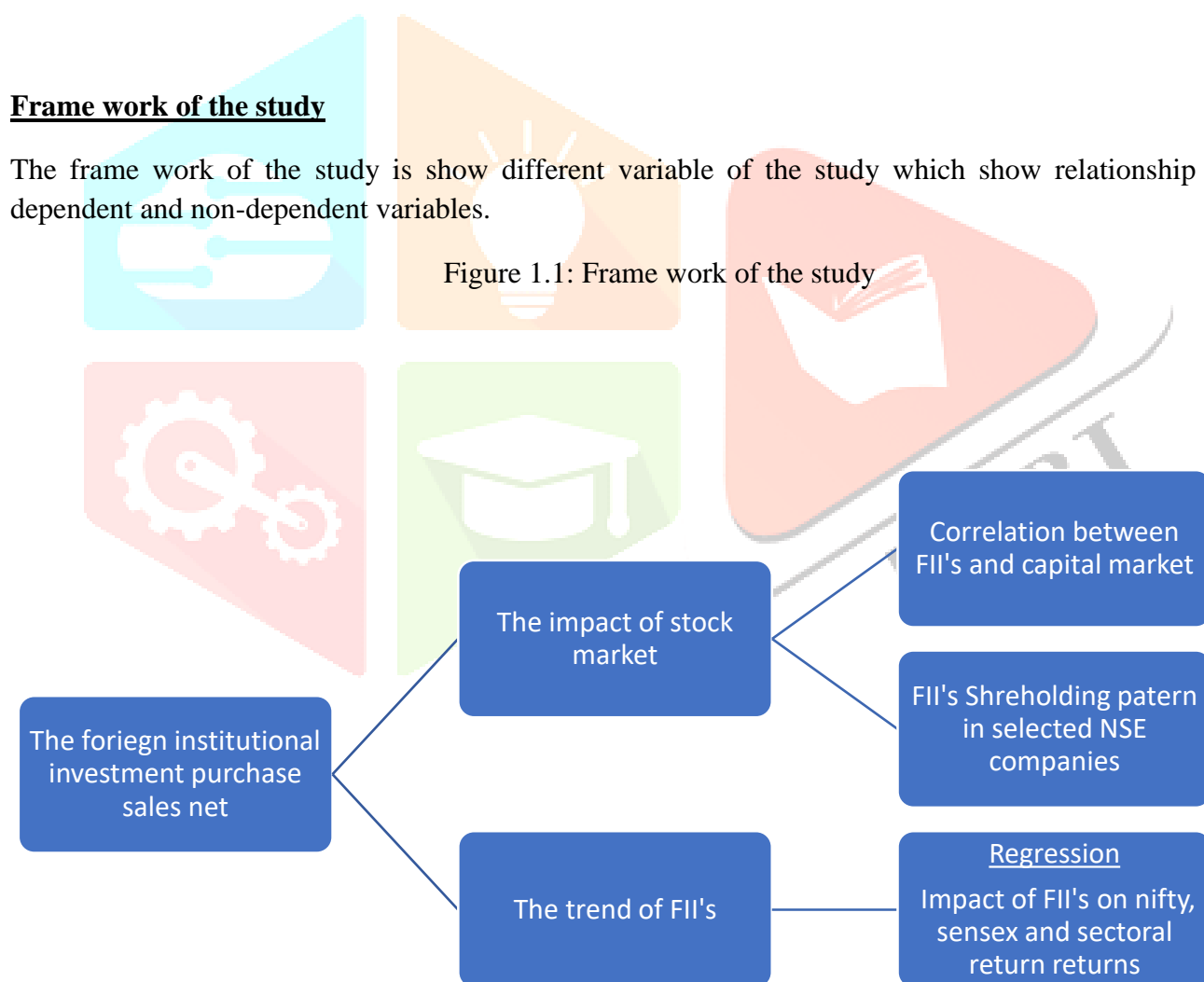
## Research Methodology

In this section, briefly presented the research methodology adopted for this study. The study variables and tools used for the study explained in details. These mentioned in the following.

Data sources and Statistical Tools the description of variables and tools used for the analysis of the data were discussed. The study is descriptive and empirical in nature and conducted based on secondary data. In this study, all the variables data collected for the period of April 2022 to March 2023 and these data collected from daily reports and monthly reports of various issues of Securities Exchange Board of India (SEBI), Reserve Bank of India (RBI), National Securities Depository Limited (NSDL ), Central Depository Service Limited( CDSL) , Bombay Stock Exchange(BSE) and National Stock Exchange (NSE) reports etc.

## Frame work of the study

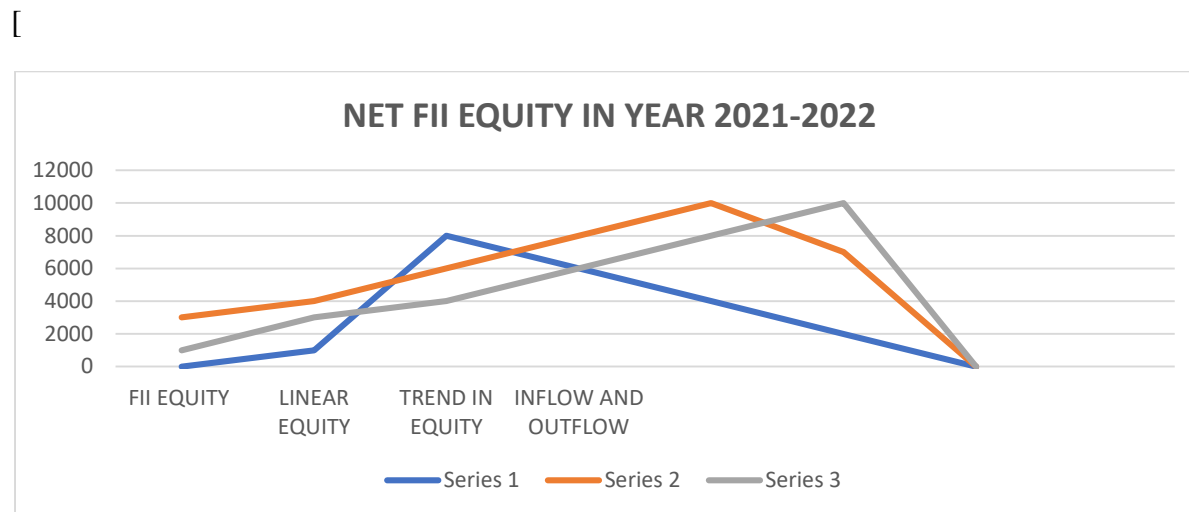
The frame work of the study is show different variable of the study which show relationship between dependent and non-dependent variables.



## Trend Analysis of Foreign Institutional Investments

The term "trend analysis" refers to the concept of collecting information and attempting to spot a pattern, or trend, in the information. The analysing trend of the foreign institutional investments will help us to capture the movements of the FIIs.

Figure: 1.2 Trend line of equity Net Foreign Institutional Investments 2021-2022



## Impact of FIIs on BSE Sensex, NSE Nifty

Period	Equity (Rs. mn.) Net	Investment (Rs. mn.)	Closing Index of BSE	NIFTY FII inflow(CR)
January	6034.75	22059.2	24439.3	5,261.70
February	16,308	15,522.60	16,330.20	7,693.10
March	21,931.00 5	20,1047	22,042.50	4,412.60
April	26,455.10	40,415.60	39,826.40	5589.20
May	49,338.20	57,585.50	24,983.10	3,535.20
June	39,845.60	38,427.40	40,830.40	4,774.00
July	23,330.60	33,014.20	39,269.70	6,231.70
August	26,782.50	30 4,578.64	47,000.40	5,431.80
September	27,591.94	40,830.40	46,808.90	4,574.50
October	24,572.22 6	50,552.60	37,419.50	3,567.8
November	49,149.30	51,574.90	40,830.40	5,623.9
December	44,701.50	54,748.50	36,410.90	4,541.9



**Table 1.1 Debt activities of Foreign Institutional Investments 2021-2022**

<b>Date</b>	<b>Gross Purchases ( Rs. Crore )</b>	<b>Gross Sale ( Rs. Crore)</b>	<b>Net FIIs ( Rs. Crore)</b>
<b>Apr- 2021</b>	<b>15,261.70</b>	<b>16,308.80</b>	<b>-1047.10</b>
<b>May- 2021</b>	<b>15,522.60</b>	<b>16,330.20</b>	<b>-807</b>
<b>Jun- 2021</b>	<b>27,693.10</b>	<b>21,931.00</b>	<b>5,762.10</b>
<b>July- 2021</b>	<b>25,589.30</b>	<b>17,377.10</b>	<b>8,212.20</b>
<b>Aug- 2021</b>	<b>26,455.10</b>	<b>22,042.50</b>	<b>4,412.60</b>
<b>Sept- 2021</b>	<b>24,160.70</b>	<b>20,056.10</b>	<b>4,104.60</b>
<b>Oct- 2021</b>	<b>25,817.50</b>	<b>29,623.10</b>	<b>-3,805.60</b>
<b>Nov- 2021</b>	<b>23,739.10</b>	<b>19,290.50</b>	<b>4,448.60</b>
<b>Dec- 2021</b>	<b>31,563.40</b>	<b>22,098.20</b>	<b>9,465.20</b>
<b>Jan- 2022</b>	<b>34,762</b>	<b>31,542.00</b>	<b>3,220.70</b>
<b>Apr- 2022</b>	<b>35,603.10</b>	<b>28,031.20</b>	<b>7,571.90</b>
<b>Apr- 2022</b>	<b>53,578.00</b>	<b>47,046.40</b>	<b>6,532.30</b>

The above Table 1.1 reveals the FII debt inflows and outflows for the financial year 2021-2022, in the year 2022-2023. FIIs gross purchases are less than the gross sales, in this period FIIs are sold debt instruments, there is more outflow of capital during this year. This is due to the governments showing interest on allowing investment in equities. This outflow trend continued up to the end of the financial year.

### **Major findings of the study**

The researcher has identified the major findings from the study presented in the following section.

1. From the study identified that the number of FIIs registered in India increased gradually, this is the sign of the strong fundamentals of the economy and also corporate earnings, accounting standards adopted according to international standards i.e., International Financial Reporting Standard (IFRS). This helps in improvement of accounting disclosure norms and corporate governance etc.
2. The majorly Foreign Institutional Investment (FII) contributed by the United States in India for the end of March 2022, this country took a share of 36 per cent in the overall FII investment in the country wise, before 2023 Mauritius has taken first place in the contribution of FII.
3. The net FII flows were found the positive in the equity market for the major period and whereas, in the debt market negative for all months during the 2022-2023. US Federal Reserve raised interest rate caused to the net sellers in the Indian debt market, in this year US Federal Reserve overnight rate more than 13 times in the year 2005-06.

### **Limitations of the study**

1. The study used secondary data and which collected from the annual and quarterly reports of the selected variables. The reliability of data depends on the published reports by the respective organizations.
2. The study conducted for selected stock market indices, of both BSE and NSE.
3. The Stock market returns are influenced by many factors, but a study conducted main consideration to FIIs investment only.
4. The FIIs shareholding pattern study conducted for the selected companies only.

### **Conclusion:**

India becomes one of the prominent emerging stock markets as a result of the various economic growth aspects of the country. The overseas investors are attracted by superior returns from the Indian stock market. The FIIs increased funds into the Indian stock market and determine the returns of Indian stock market; and also causes the fluctuations in major Indian stock indices of both BSE Sensex and NSE Nifty. The Net FIIs investment impacted greater on the NSE Nifty in comparison to BSE Sensex. The stock market returns in the study proved, the greater risk involved for higher returns. The study found that, FIIs held maximum holding in the non-governmental scrips than the governmental. Scope for further Research There is a

satisfactory extent of undertaking further research on Foreign Institutional Investments and related issues. The study is interesting to compare the Shareholding pattern of the FIIs and Domestic Institutional investors (DIIs) in the Indian companies. The study much interested to in FII derivative market, which is become popular in the modern context.

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