Determinants of FIIs Net Investment in India

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Abstract*: *Indian stock market has witnessed spectacular change in the recent decade. The market has undergone huge reform in the past few years. The linkage of stock market with macroeconomic variables has always been an area of interest among investors and policy makers. The stock market and its indicators in the form of indices, reflect the potential, the direction and health of the economy. There is an extensive group of macroeconomic variables that influences the stock prices in the share market. The stock market of emerging economy like India carries huge expectation of the investors. The Indian stock market improves with the increase in the inflow of foreign investment. FIIs investment is volatile by nature and also FIIs flows have positive and negative impact in the market as well as the economy. Hence, there is a need to determine the push and pull factors behind any change in the FIIs, so that it will become easy to frame the policies by considering the variables that attract foreign investment.. It becomes really important for any investor to understand the key economic factors which have high influence on FIIs investment Indian stock market improves with the increase in the inflow of foreign investment. Hence, there is a need to determine the push and pull factors behind any change in the FIIs, so that it will become easy to frame the policies by considering the variables that attract foreign investment. The foreign investor's participation in Indian stock market increases the liquidity of local markets and lowers the cost of capital. It becomes really important for any investor to understand the key economic factors which have high influence on FIIs investment. Hence, an attempt has been made to analyse the factors determining behaviour of FIIs net investment.

Keywords* : *FDI,.

I. INTRODUCTION

Indian stock market has witnessed spectacular change in recent decade. The market has undergone huge reform in the past few years. The linkage of stock market with macro economic variables has always been an area of interest among investors and policy makers. The stock market and its indicators in the form of indices, reflect the potential, the direction and health of the economy. There is an extensive group of macro economic variables that influences the stock prices in the share market. The stock market of emerging economy like India carries huge expectation of the investors. The Indian stock market improves with the increase in the inflow of foreign investment. Thus foreign investment as well as money supply exhibits its significant positive impact on the stock market.

STATEMENT OF THE PROBLEM

FIIs investment is volatile by nature and also FIIs flows have positive and negative impact in the market and economy. Hence, there is a need to determine the push and pull factors behind any change in the FIIs, so that it will become easy to frame the policies by considering the variables that attract foreign investment. The foreign investor's participation in Indian stock market increases the liquidity of local markets and lowers the cost of capital. It becomes really important for any investor to understand the key economic factors which have high influence on FIIs investment. Hence, an attempt has been made by the researcher to analyse the factors determining behavior of FIIs net investment.

II. OBJECTIVES OF THE STUDY

1. To find out the factors affecting FIIs flows in India.
2. To examine the relationship between FIIs and others economic factors like stock market, foreign exchange reserves, exchange rate and inflation.

III. HYPOTHESIS

- The economic fundamentals such as stock market return, exchange rate, foreign exchange reserves, and inflation rate do not affect the flows of FII in India

IV. REVIEW OF LITERATURE

Amita (2014), "Determinants of FIIs: Evidence from India", the present paper is aimed to identify the determinants of Foreign Institutional Investment and to establish a relationship between them. The economic variables used are Foreign Exchange Rates, BSE Sensex, Exchange Rates, and Inflation. Secondary data has been used for a period of 12 years from 2001-02 to 2012-13. The data was obtained on monthly basis. Econometric tools like Augmented Dicker Fuller test and Granger Causality Test are used to analyse the data. The correlation coefficient between FIIs and Sensex, FIIs and FERs, FERs and Sensex, and WPI and Sensex were found positive. However, exchange rates and Inflation was found having negative relationship with FIIs. The results of Granger Causality Model indicated bidirectional causality between FII and Sensex, and FII and Exchange rate. However, no causality was found between FII and Foreign Exchange Reserves.

T Mohanasundaram, P Karthikeyan, V Krishnamoorthy (2015), "Macroeconomic Dynamics of Foreign Institutional Investments in India", the authors study the determinants of Foreign

Revised Manuscript Received on September 25, 2019

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Institutional Investments (FII) in India using monthly time series data for the period from April 2001 to March 2014.The secondary data have been collected from officially published websites. Correlation and Autoregressive Distributed lag (ARDL) bounds testing approach have been used. The authors have found that FII flows are having positive relationship with Exchange Rate, Producer Price Index of USA, Return on S&P 500, Return on Nifty, and Market Capitalization of NSE and having negative relationship with Wholesale Price Index of India. The result of ARDL model shows that the US 3-month T-bill rate (USTBR) representing foreign interest rate has significant and negative impact on FIIs investment in host (Indian) stock market and Producer Price Index (PPI) of USA has significant and positive influence on FIIs flows in the Indian stock market at long run. It is concluded that FII inflows to India are primarily determined by macroeconomic factors.

V. RESEARCH METHODOLOGY

This study aims at, analyzing the relation between the FII flows and others economic variables such as stock market, foreign exchange reserves, exchange rate and inflation. Data for the study will be secondary in nature and the period of study 2007-08 to 2017-18.

DETERMINANTS OF FIIS NET INVESTMENT IN INDIA

Foreign institutional investment can supplement domestic savings and augment domestic investment without increasing the foreign debt of the country. Such investment constitutes non-debt creating financial instruments for the current account deficits in the external balance of payments. The behaviour of the FIIs depends on so many factors. These factors can be classified into international factors and domestic factors. International factors are international market capitalisation, exchange rate variance, foreign interest rate, foreign industrial production, international crisis. Domestic factors are market return on investment in shares, variance of return in stock market, beta of the stock market, information asymmetry, impact cost, non-promoter share holdings, domestic credit rating, domestic companies P/E ratio, infrastructure facility, and macro economic factors. Though there are many economic variables which provide indication on the economic development of the country, it is not necessary that all those economic variables play an eminent role in influencing FIIs flows. Hence, an attempt has been made to know the list of key macro economic variables which have greater stimulus in determining FIIs flows. The various macro economic factors of the countries also affect the FIIs volume in a country. These variables are GDP growth rate, Inflationary rate, Interest rate and the like. The Indian economy slowed significantly during 2011-12, with growth decelerating to 6.5 per cent. The GDP growth for 2012-13 and 2013-14 remain weak due to a combination of weak global and domestic macro economic factors. GDP, foreign exchange reserves, interest rate, currency fluctuation against US Dollar, balance of payments and inflation are some of the important factors which are greatly influencing the economic growth which in turn will influence the FIIs flow to India.

GROWTH OF FIIs NET INVESTMENT:

FIIs net investment for the study period is presented in Table 1.

Table 1:FIIs Net Investment in Equity (2008 – 09 to 2017 – 18)

Years	FIIs Net Investment (₹. n billion)	Nifty Index
2008-09	-458	3021
2009-10	1427	5249
2010-11	1464	5834
2011-12	937	5296
2012-13	1684	5683
2013-14	450	6704
2014-15	2775	8491
2015-16	-182	7738
2016-17	484	9174
2017-18	1451	10114

Source: ISMR, SEBI

It is observed from Table 1 that FIIs net investment during the period was high (Rs.2775 bn) in the year 2014-15 and it was low(Rs.-458bn) in the year 2008-09. The net investment increased by more than 5 times from 450 billion in the year 2013-14 to 2775 billion in the year 2014-15. This abnormal growth in FIs net investment is due to their confidence on the new Union Government under the headship of Mr.Narendra Modi. In 2015-16 the Nifty have fallen from 8491 to 7738 and then recovered quickly in the year 2016-17. After that the Nifty have been gradually increased to 10114 in the year 2017-18.

VI. CORRECTION ANALYSIS

Table 2 Correlation coefficients of FII and its determinants

	FII	Sig.
GDP	-0.139	0.684
Foreign Exchange Reserves	0.373	0.258
Currency Fluctuation	0.231	0.493
Interest Rate	-0.491	0.126
Inflation	0.522	0.100
Balance of Payment	0.022	0.950

The above table shows that the p value of all Foreign exchange reserves, Interest Rate and Inflation are less than 0.05, $p < 0.05$, therefore the hypotheses set for these variables are rejected at 0.05 level of significance and a significant relationship is found between FII inflows and these variables; whereas for GDP and Balance of Payment , $p > 0.05$, therefore the null hypotheses is accepted.

VII. CONCLUSION

Foreign capital is considered to be a vital component for the economic growth of a developing country. Since 1990's to this date the Government of India has eased its foreign capital policies and norms and many initiatives to attract foreign capital has been implemented. It is found that the FII inflows have increased for the period under study and exhibits an upward trend. FIIs inflow influence the stock market directly. The test result also proved that FIIs inflow is not affecting the stock market through macro economic factors.

ACKNOWLEDGEMENT

I hearty thank to the Department of International Business in Alagappa University. This research work was partially sponsored by RUSA 2.0 scheme of MHRD in Alagappa University, Karaikudi.

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