

## Foreign Institutional Investment (FII) and Growth of Indian Capital Market

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### Abstract

Foreign Institutional Investors are very significant investors in Indian economy and getting a stable and long term acceptance in the country. As of now the capital market of the country is moved by the FIIs to a certain extent as they are very active in terms of investment and at times, fluctuation in the share prices are governed by FIIs. All this started from the announcement of industrial and economic reforms in 1991 when a number of foreign and private investors hit the Indian economy. This study is an attempt to evaluate the impact of FIIs on the Indian capital market. The period of study is 19 years i.e. 2000 to 2018 and correlation analysis is used to analyze the data.

**Keywords:** FIIS, NIFTY, SENSEX, Indian Capital Market.

### Introduction

Any institution from outside India which is interested to invest in Indian securities market can be stated as Foreign Institutional Investor of FII. The investment activities of all such FIIs are governed and regulated by SEBI and particularly according to Sec. 2 (f) of SEBI, incorporated in 1995. Foreign institutional investment started in India after the announcement of Industrial Policy 1991. As a result, the drive of Liberalization, privatization and Globalization became the main stream investment system of the country. By the year 1992 a number of Foreign Institutional investors entered India in the form of Mutual funds, investment trusts and even asset management companies, beyond this time period other type of investments in trusts, foundations and even endowment also started.

In the present scenario, FII are the important investors in Indian economy and getting a stable

and long term acceptance in the country. As of now the capital market of the country is moved by the FIIs to a certain extent, as they are very active in terms of investment and at times fluctuation in the share prices are governed by these FIIs. This can be said in the light of the fact that most of the stocks of Indian origin are not traded in a frequent manner, provided more than 4000 such companies are listed, but the stocks of FIIs are traded very actively.

Some of the adjoining events related to the growth of FIIs in India can be stated as follows:

- In 1992 FIIs were allowed in the Indian stock market, tools were shares and debentures. This condition stands true for all the listed and be listed companies.
- The allowed limit of holding was 24% of the total issued capital, but with a condition that none of the members is holding more than 5% of the total investment.
- In 1996, 100% investment was allowed in case of debt securities, though it required prior approval of SEBI, and the limit of total investment was USD 1.53 Billion.
- Then in 1997 SEBI allowed the FIIs to invest 30% of their issued capital which was 24% till 1992.
- Then in 1998, FIIs were allowed to invest in the old government securities and even in the treasury bills.
- By the year 2000 even the corporates were allowed to invest as sub-account of FIIs provided they are registered with SEBI. Also the portfolio investment was raised to 49% as per the raise in sectorial cap.
- In 2004 the cap of investment was raised to USD 1.75 Billion from the previous cap of USD 1 billion.
- The cap of overseas investment was increased to INR 1, 30, 000 Cr. from 2016.

The funds in which FII is allowed can be listed as follows:

- Endowment
- Banking
- Insurance
- Trusts
- Charity (Trust and Societies)
- Mutual funds

- Pension Funds

Then there are certain kind of business where the FIIs are not allowed, like:

- Chit Fund Companies
- Bachat and Nidhi agencies
- Agriculture
- Real Estate (some parts only)
- TDRs

### **Guidelines of SEBI for FIIs**

- All the FIIs are required to get registered with SEBI and obtain the certificate of registration, where all the business related information is required to be furnished.
- Approval against FERA (1973) is also required from RBI,
- In every three years the above said certificate of registration is required to renewed,
- SEBI allows all the FIIs to invest in both the primary and secondary markets where they can deal with shares, Debentures, securities, etc.
- The respective fee of registration is USD 10, 000 and is application of 3 years of time.
- Registered FII can list in all the approved stock exchanges of the country.

As it is clear from the above given matter that in the present scenario, FIIs are the integral part of Indian capital market, and these Foreign institutional investments are having a great impact on Indian capital market. This present study will evaluate this impact and also analyze the future trends of growth in this concern.

### **Literature review**

**Gupta et al (2013)** conducted a study on the inflow from FIIs in Indian capital market. The study was conducted on the FIIs listed on the BSE. The respective findings of the study stated that there is a positive relationship between the overall growth of FIIs in the country and capital market. Though the relationship is causal in nature but the effect of the same is positive on BSE.

**Bansal et al (2015)** conducted a study based on the evaluation of market behavior with respect to capital market of India. As a matter of fact this was an empirical analysis and the findings of the study stated that after the entry of FIIs in the Indian capital market, the market has become more

volatile. Then on the other hand the findings also suggest that there was no major change on the overall returns of the market if FIIs are included.

**Shukla (2017)** conducted a study based on the FIIs investment in Indian stock market and the study was based on the evaluation of data on daily basis. The said study period was 10 year i.e. 2001 to 2010. Multiple correlation analysis was used as a tool of analysis. The findings of the study stated that the investments from FIIs are having a positive impact in Indian capital market and the stock index on daily basis. The findings also suggested that the degree of variation is different for different sectors of the economy.

**Banerjee (2017)** conducted a study based on the inflow from FIIs in Indian capital market and impact of this inflow on Indian stock market. Findings of the study stated followed by the announcement of LPG policy in 1991 there was no turning for the public sector enterprises including banks. As a matter of fact the Indian Stock market started to experience a major volatility and this volatility was due to the entry of FIIs in the market. In the present scenario, indirectly, the stock prices are decided by FIIs and there is no agency India who can deny the fact that FIIs are the integral part of Indian economic system.

### **Objective**

The objective of this study is to analyze the relationship between Foreign Institutional Investment (FII) and growth of Indian Capital Market.

### **Hypothesis**

H<sub>0</sub>: There is no significant relationship between investments from FIIs and growth of Indian Capital market.

H<sub>1</sub>: There is a significant relationship between investments from FIIs and growth of Indian Capital market.

### **Research Methodology**

#### ***Type of Research***

This study is exploratory in nature as the researcher is trying to investigate the relationship between stated variable and perform the analysis. Data is of secondary nature because the events have taken place in the past and is being evaluated in the present and published data is

**authentic. Sources of Data**

As stated above, this study is based on secondary data and the researcher has approached a number of secondary sources, some of the notable sources are:

- Official Websites of NSE and NIFTY
- Research article from national and international journals
- Monthly records of selected companies

**Statistical Tools**

- Basic descriptive statistics tools like average, percentage, etc.
- Correlation analysis
- Student 't' Distribution.

**Period of Study**

The respective period of study is 19 years i.e. 2000 to 2018.

**Data interpretation and analysis****Table 1: Year Wise Investments from FIIs (2000 to 2018)**

Year	Net FII (In Cr.)
2000	6419
2001	6510
2002	11324
2003	2987
2004	31081
2005	39651
2006	40418
2007	64991
2008	43185
2009	73491
2010	94187
2011	46882
2012	129226
2013	83462
2014	197221
2015	71664
2016	108815
2017	113490
2018	154436

Source: [www.indianexpress.com](http://www.indianexpress.com)

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As can be seen from the table of Net FII from 2000 to 2018 it can be seen that from 2001 to 2010 the rate of increase in net FII is around 150% and in the next 8 years there was a high turmoil in the rate of growth. The increase in the growth rate was because of policy decision of SEBI where the limit of FII investment has increased and even the limit of share percentage has also increased. The on the other hand, the entry of new FIIs has boosted the overall market as well..

**Correlation analysis**  
**Correlation between FIIs and SENSEX**

<b>Descriptive Statistics</b>			
	<b>Mean</b>	<b>Std. Deviation</b>	<b>N</b>
<b>FII</b>	73150.00	570.281	20
<b>SENSEX</b>	62692.10	482.085	20

<b>Correlations</b>			
		<b>FII</b>	<b>SENSEX</b>
<b>FII</b>	Pearson Correlation	1	.704**
	Sig. vale at 5% level		.000
	Sum of Squares	243453.000	276965.000
	Combined var.	1281.010	1457.334
	Sample	20	20
<b>SENSEX</b>	Correlation	.704**	1
	Sig. vale at 5% level	.000	
	Sum of Squares	276965.000	552977.053
	Combined var.	1457.474	2910.253
	Sample	20	20

**Interpretation**

The correlation analysis between the FIIs and SENSEX shows that the correlation between the two is 0.704, this is an indication that there is a strong and positive correlation between the two components. It can also be interpreted that the entry of new FIIs in the Indian capital market is an independent variable and the growth of SENSEX is dependent variable. It has been observed from the trail of secondary data that during the study period SENSEX has grown by 60.34% and this can be result of successful operation of FIIs in the Indian capital market.

**Correlation between FII and NIFTY  
Descriptive Statistics**

	Mean	Std. Deviation	N
<b>FII</b>	6834250.00	277796.538	20
<b>NIFTY</b>	1498075.00	127027.051	20

<b>Correlations</b>			
		<b>FII</b>	<b>NIFTY</b>
<b>FII</b>	Pearson Correlation	1	0.609
	Sig. vale at 5% level		.528
	Sum of Squares	23151.000	39964.000
	Combined var.	771.667	665.231
	Sample	20	20
<b>NIFTY</b>	Correlation	0.609	1
	Sig. vale at 5% level	.528	
	Sum of Squares	49961.000	48407.000
	Combined var.	1665.333	1613.667
	Sample	20	20

### Interpretation

The correlation analysis between the investments from FIIs and growth of NIFTY is given in the above table and the respective coefficient of correlation is 0.609 which is a moderate degree of positive correlation. This is an indication that there is a direct relationship between the growth of Indian capital market and investments from FIIs and the overall market capitalization is dependent on these investments to a certain extent. The respective values are tested on the 95% level of significance.

### 't' test for Hypothesis Testing

Test Statistics:  $t = r \sqrt{\frac{n-2}{1-r^2}}$

According the above given

data, n 20, 0.609

$$.472 \sqrt{\frac{20-2}{1-0.609^2}}$$

then,

$$= 5.994$$

The 't' test statistics falls in the rejection region, hence the result is not favorable.

### Result

Since at 2 degrees of freedom for 2 tailtest the table value at 0.05 critical limit is 4.30 which is less than the calculated value of 't' so the null hypothesis 'There is no significant and direct relationship between investments from FIIs and growth of Indian Capital market' is rejected and it can be stated that the growth of Indian capital market significantly depends on the investments from FIIs..

### Conclusion

After the launch of industrial reforms in 1991 the Indian capital market has undergone a number of changes and by the way of liberalization and globalization a number of foreign and private investments hit the Indian economy. Getting a head start in 1995, in the present scenario the average closing price is influenced by FIIs to a great extent. Then on the other hand the favorable policies of SEBI and RBI have given a chance to FIIs so as to flourish



in India as such. As a result there is more than 200% of growth in investments from FIIs since 1995.

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