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# "IMPACT OF FOREIGN INSTITUTIONAL INVESTMENT ON BSE SENSEX"

Commerce

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## ABSTRACT

Being a developing Country, India attracts a large sum of FII every year. These foreign investments have a great impact on the economy of India. Indian Stock Market, which is one of the indicators of the economic status, is also being affected by the foreign investments. Foreign institutional investors have gained a significant role in Indian stock markets. The dawn of 21st century has shown the real dynamism of stock market and the various benchmarking of sensitivity index (Sensex) in terms of its highest peaks and sudden falls. In this context the paper examines the contribution of foreign institutional investment in sensitivity index (Sensex). It also attempt has been made to examine the volatility of BSE Sensex due to FII during the period of 2012 to 2017. The data for the study uses the information obtained from the secondary resources like website of BSE and money control. An attempt has been made to explain the impact of foreign institutional investment on BSE. Sensex.

## KEYWORDS

### Introduction

The liberalization policies initiated in India in the early 1990s brought about radical changes in the conduct of stock market. Indian stock market opened to Foreign Institutional Investors on 14th September 1992, initially with lot of restrictions. The regulation on FII are liberalized and minimized, since 1993 the market has received a considerable amount of portfolio investment from foreigners in the form of FIIs investment in equities. This has become a turning point of India stock market. The government of India came out with the policy to permit the FII investment in Indian capital market. Rising globalization, deregulation, and foreign portfolio investments made the Indian stock exchanges competitive and efficient in their functioning. With the rise of equity culture across the globe, even India which has a long history of stock exchanges, has witnessed a perceptible shift in the proportion of investor's participation in equity markets.

### Statement of the Problem

With the advent of globalization, there have been massive Foreign Institutional Investment (FII) flows into emerging equity markets like India. Foreign Institutional Investors (FIIs) were permitted to invest in all the listed securities traded in Indian capital market for the first time in September, 1992. As a result of abolishment of barriers to capital inflows in the form of FIIs investment, India attracted huge amount of foreign capital particularly from developed countries. International capital inflows have both positive as well as negative impact on the health of the recipient economy. On the positive side, these capital inflows raise the level of economic development. But these capital inflows also pose several threats to the domestic economic and financial system of the recipient economy like inflation and possibility of sudden withdrawal.

Therefore, we must consider the risk factor in terms of foreign investment volatility. The term volatility is concerned with the international investors′ intention to invest for short-term benefits and they withdraw their investment on uncertain conditions. Hence, an attempt has been made to analyze the impact of foreign institutional investors in Indian stock market.

### Objectives of the Study

- To find out the relationship between the FIIs investment and BSE Sensex.
- To know the volatility of BSE Sensex due to FII investment.

### Tools

- Trend Analysis
- Descriptive Statistics
- Correlation
- Regression

### Limitation of the study

As the time available is limited and the subject is very vast and it focused only on identifying whether there exist a relationship between FII equity & Debt investment and BSE Sensex. The data used for analysis is historical in nature.

### Review of Literature

| AUTHOR | SAMPLE RESPONDENTS | OBJECTIVE | TOOLS | FINDINGS |
|---|---|---|---|---|
| Arshanapalli Bala et al (1997)1 | The sample data consisted of daily closing prices for the three indices from January 1991 to December 1998 with 2338 observations | The research examined the nature and extent of linkage between the U.S. and the Indian stock markets. | Correlation | The results were in support of the intuitive hypothesis that the Indian stock market was not interrelated to the US stock markets for the entire sample period. It should be noted that stock markets of many countries became increasingly interdependent with the US stock markets during the same time period. |
| Kumar (2001)2 | The sample data represented by the Sensex using monthly data from January 1993 to December 1997 | The research investigated the effects of FII inflows on the Indian stock market | Regression | FII strongly influence short-term market movements during bear markets. However, the correlation between returns and flows reduces during bull markets as other market participants raise their involvement reducing the influence of FIIs. |
| Gordon and Gupta (2002)3 | They used the data from September 1992 till October 2001 | The study conducted portfolio flows in India and the influence of domestic fundamental factors. | Regression model and Unit root test | It was concluded that the portfolio flows to India are small, compared to other emerging markets and also less volatile. |

| | | | | |
|---|---|---|---|---|
| Karimullah (2007)4 | The data used for the period of January, 1997 to June, 2007. | The Research examined the impact of Foreign Institutional Investors' (FII) equity investment behaviour in the Indian stock market. | Granger Causality Test | The result indicated that stock market performance is a major determinant of both the FIIs |
| Karan Walia Et Al. (2012)5 | The sample data represented by the Sensex using monthly data from April 2008 to March 2012. | Impact of foreign institutional investment on stock market and Indian economy. | Karl Pearson' Coefficient of correlation test, Correlation. | It was found that the FIIs were influencing the Sensex movement to a greater extent. Further it was evident that the Sensex had increased when there was positive inflow of FIIs and vice versa. |
| Hemkant Kulshrestha (2014)6 | The data observed that investments by FIIs and the movements of BSE Sensex and CNX Nifty | The study explained impact of FII on Indian Stock Market. | Correlation | Foreign institutional investors (FIIs) had significant impact on the movement of Indian capital market. |

**Analysis and Interpretation**

**Table No. 1 – Trend Analysis of Equity and Debt of FII and Movement of BSE Sensex during 2012-2017**

| YEAR | FII - EQUITY | TREND % | FII - DEBT | TREND % | BSE SENSEX | TREND % |
|---|---|---|---|---|---|---|
| 2012-2013 | 140032.6 | 0 | 28334.4 | 0 | 18835.8 | 0 |
| 2013-2014 | 79708.5 | -43.08 | -28060 | -199.03 | 22386.3 | 18.85 |
| 2014-2015 | 111332.6 | 39.67 | 166127 | -692.04 | 27957.5 | 24.89 |
| 2015-2016 | 14171.6 | -87.27 | -4003.8 | -102.41 | 25341.9 | -9.36 |
| 2016-2017 | 55702.6 | 293.06 | -7291.6 | 82.12 | 29620.5 | 16.88 |

Source: www.Sebi.gov.in

**Chart No. 1 - Equity and Debt of FII and Movement of BSE Sensex during 2012-2017**

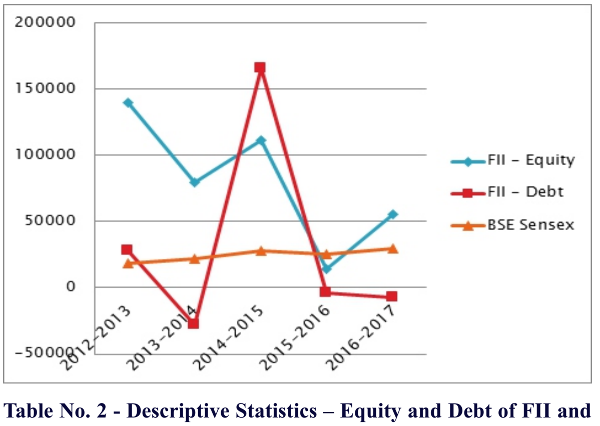


**Table No. 2 - Descriptive Statistics – Equity and Debt of FII and Movement of BSE Sensex**

| Variables | N | Mean | Standard deviation |
|---|---|---|---|
| BSE Sensex | 5 | 2.4 | 4327.08 |
| FII - Debt | 5 | 3.1 | 78176.11 |
| FII - Equity | 5 | 7.4 | 58937.00 |

The above table reveals that mean of the data and the significant standard deviation of data .The mean value for the sample data FII's equity is 7.4 and the standard deviation for the same is 58937. The mean value for the sample data FII's Debt is 3.1 and the standard deviation for the same is 78176.11. The mean value for the sample data BSE Sensex is 2.4 and the standard deviation for the same is 4327.08. The mean value for the sample data Net FII's Investments is 1.8 and the standard deviation for the same is 9588.86

**Table 3 - Regression Analysis – Relationship between FII equity Investments and BSE Sensex**

Ho: There is no significant impact of FII equity investments on BSE Sensex

| Coefficientsa | | | | | | |
|---|---|---|---|---|---|---|
| Model | | Unstandardized Coefficients | | Standardized Coefficients | T | Sig. |
| | | B | Std. Error | Beta | | |
| 1 | (Constant) | 24344.190 | 2345.323 | | 10.380 | 0.002 |
| | Equity | 0.016 | 0.031 | 0.282 | 0.509 | 0.646 |

a. Dependent Variable: BSE Sensex

It is inferred from the regression table that FII equity investments affects the BSE Sensex during the study period. T test reveals that significant value (0.646) is greater than the significant value (0.05). Hence, the null hypothesis is accepted and there is no impact of FII equity investments on BSE Sensex.

**Table 4 - Regression Analysis – Relationship between FII debt Investments and BSE Sensex**

Ho: There is no significant impact of FII debt investments on BSE Sensex

| Coefficientsa | | | | | | |
|---|---|---|---|---|---|---|
| Model | | Unstandardized Coefficients | | Standardized Coefficients | T | Sig. |
| | | B | Std. Error | Beta | | |
| 1 | (Constant) | 27112.065 | 3516.086 | | 7.711 | 0.005 |
| | Debt | -0.31 | 0.039 | -0.417 | -0.796 | 0.484 |

a. Dependent Variable: BSE Sensex

It is inferred from the regression table that FII debt investments affects the BSE sensex during the study period. T test reveals that significant value (0.484) is greater than the significant value (0.05). Hence, the null hypothesis is accepted and there is no significant effect of FII debt investments on BSE Sensex.

**Table 5 - Correlation Analysis - Relationship between BSE Sensex and FII**

Ho: There is no significant association between BSE Sensex and FII.

**Correlation**

| | | |
|---|---|---|
| BSE Sensex and FII | Pearson Correlation | .250 |
| | Sig. (2 tailed) | .216 |
| | N | 5 |

The correlation provides a measure of association between BSE sensex and FII investment. Correlation is 0.250 which indicates that there is a low level of positive association between BSE Sensex and FII investment. It is inferred that significant value (0.216) is greater than 0.05, hence null hypothesis is accepted and there is no significant association between BSE Sensex and FII.

**Suggestions**

**Mode of investment:**

Foreign institutional investors have two way of investment for investing in Indian capital market, one way is debt investment another one way is equity investment, though debt investment opened in 1997, FIIs did not show full interest as they have mostly invested through equity, and investment in debt by FIIs in the sample period of this study is not convincing compared to equity investment. So there is need to further rationalize the policies and regulations of debt investment for FIIs. It will also be helpful in attracting more investment in debt segment by the FIIs.

**Improving Capital Markets:**

FII' as professional bodies of asset managers and financial analysts enhance competition and efficiency of financial markets. By increasing the availability of riskier long term capital for projects, and increasing firms' incentives to supply more information about them, the FIIs can help in the process of economic development.

**Investors:**

The government should simplify procedures and relaxing entry barriers for business activities and providing investor friendly laws and tax system for foreign investors. The laws should be such that it should protect domestic investors and also promote trade in country through FIIs. It will lead to increase foreign investors and domestic investors.

**Government:**

Government should understand the behavior of FIIs in the Indian stock market that will help them to decide their policy initiatives to attract funds from FIIs in the Indian stock market. FII help in equity market development that contributes towards the economic growth of the country. Government should set a minimum limit as well as maximum limit, within which FII could invest in India, in order to avoid volatility in Indian stock market.

## Conclusion

Domestic sources of finance are limited in many countries, particularly those with emerging markets. Through capital market liberalization, foreign capital has become increasingly significant source of finance. In developing countries like India foreign capital helps in increasing the productivity of labour and to build up foreign exchange reserves to meet the current account deficit. Foreign Investment provides a channel through which country can have access to foreign capital. There are speculations of wider range on the expectations of foreign institutional investors. It is required to understand when they withdraw their funds and when they pump in more money. Higher sensex indices and high price earnings ratio are the country level factors attracting more foreign investment in India.

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