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AN EMPIRICAL STUDY ON THE ROLE OF FOREIGN INSTITUTIONAL INVESTORS IN DEVELOPING COUNTRY LIKE INDIA

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ABSTRACT:

Foreign Institutional Investments (FIIs) definitely boost the Indian economy, but before we learn how FIIs can help boost the Indian economy, it is important to understand what FIIs are. Foreign Institutional Investors are essentially investors or investment companies that are not located within a country or area in which they are investing. In layman's terms, they are outsiders in the financial markets of a particular country. FII is a common term in the financial sector in India although it is not as frequently used as FDI.

In fact, many people confuse FIIs with Foreign Direct Investments (FDIs). FDIs are usually associated with the growth of exports whereas FIIs are monies which chase stocks in the market. Also, FDIs are permanent in nature whereas FIIs fly away at the slightest economic or political disturbance.

KEYWORDS: *FII, Boost Indian Economy, Financial Markets, FDI.*

INTRODUCTION:

Foreign institutional investors are entities which are established or incorporated outside India and make a proposal for investment in India. These proposals are basically made by the foreign institutional investors on behalf of the sub-accounts, which may include foreign corporates, individuals, funds etc.

In order to act as a banker to the foreign institutional investors the reserve bank of India (RBI) has enrolled banks that are authorized to deal with them. The biggest source through which foreign institutional investors invest in the issuance of participatory notes (p- notes) which are also called as offshore derivatives.

Foreign Institutional Investors (FII) in India

Countries with the highest volume of foreign institutional investments are those that have developing economies. These types of economies provide investors with higher growth potential than in mature economies. This is why these investors are most commonly found in India, all of which must register with the Securities and Exchange Board of India to participate in the market.

Regulations for investing in Indian companies

All foreign institutional investors are allowed to invest in India's primary or secondary capital market only through the company portfolio investment scheme (PIS) these schemes are allowed the foreign institutional investors to purchase shares and debentures of Indians companies on the normal public exchanges in India.

For eg- United States mutual fund sees an opportunity of investment in Indian based company so it can purchase the equity on the Indian public exchange and take a long position in a high growth stock. This thing also helps the domestic private investors who may not be able to register with the securities and exchange board of India (SEBI)

Be that as it may, there are numerous directions incorporated into the plan. There is a roof for all FIIs that express the maximum speculation sum must be 24% of the paid-up capital of the Indian organization getting the venture. The maximum speculation can be expanded above 24% through board endorsement and the death of an extraordinary goal. The roof is decreased to 20% of the paid-up capital for interests out in the open segment banks.

OBJECTIVES:

- To understand the concept of FII
- To understand the role of FII in developing nations like India.
- To understand advantages and limitations of FII
- To understand the norms associated with FII.

The advantages and disadvantages of FII

Advantages

Enhanced flow of capital

It increases the growth rate of the investment whereby development project, economic and social infrastructure is built in which it boost the production and employment and income of the country.

Managing uncertainty and control

It helps in promoting a hedging instrument and also improve the competition in a financial market also an alignment of assets which helps in stabilizing the market.

Improved corporate governance

The foreign institutional investors build professional bodies like a financial analyst who through their contribution to better understanding and improves the firm's operation and corporate governance and solve the problem of an agent.

Disadvantages

Since foreign institutional investors are controlled by investors which cause sudden outflow from markets leading to a shortage of funds.

Inflation

Huge inflow of foreign institutional investors funds creates high demand for the rupee and whereby pumping huge amount of money by the RBI into the market. This creates excess liquidity creating inflation.

Adverse impact on exports

With Foreign institutional investors inflows leading to an appreciation of the currency, exports become expensive which ultimately leads to lower demand and hence shortfall in the export of goods and reduce the competitiveness.

These are certain myths about the FII

- It never unlisted the entities and only participate in stock and exchange
- It invests during initial allotment of shares but cannot invest at the time of allotment
- It does not generally influence the management of enterprise and is mostly interested in capital gains and monetary price differences, unlike FDIs who invest directly in technology & management.

FOREIGN INSTITUTIONAL INVESTORS IN INDIA

Yes, foreign institutional investors can invest in Indian companies in stock and debenture. They have to trade through the portfolio investment scheme for investing in the primary and secondary capital market in India. According to the regulations of reserve bank of India (RBI), the overall investment for foreign institutional investors is only 24% of the paid up capital of the Indian companies. In the case of public sectors the limit is 20% paid up capital but if the board and general bodies approve and passes a special resolution then investment can be raised up to 24% for the particular segment.

Over the years, emerging markets, including India, have become hot investment destinations for foreign institutional investors because of their huge growth potential. The Securities and Exchange Board of India has more than 1400 foreign institutional investors registered with it and this figure is likely to increase in the next few years. Institutions involved in FIIs are mutual funds, hedge funds, pension funds, university funds, foundations, endowments, charitable societies, and insurance companies.

FIIs have a huge impact on the Indian economy – a sudden influx of FII can essentially drive the stock market. In fact, a large part of the 25% (plus) rally in Sensex in 2012 can be attributed to the Rs 1.23 trillion (US$ 20 billion) of inflow from FIIs. Additionally, FIIs lower the cost of capital and provide access to cheap global credit.

Recently, reports surfaced that after a reduction in the bond buying program by the US Federal Reserve, India witnessed a sharp decline in the Indian equities by over Rs 2,000 crores. In fact, after the US Federal Reserve made this announcement, foreign investors withdrew Rs 2,000 crores from Indian equities within a fortnight.

HOW CAN A FII INVEST IN INDIA

There are so many entities which want to invest in Indian capital market under the foreign institutional investor's routs. So these markets want to invest as FIIs or as sub-accounts. These are the following points.

- Mutual funds, Investment trust, asset management company, nominee company, overseas pension funds bank, institutional portfolio manager, university funds, endowments, charitable trusts, foundations, charitable societies, a trustee or power of attorney holder incorporated or established outside India intending to make proprietary investments are all examples of investments which can be termed as foreign institutional investments.
- Sub account- basically sub-account is an underlying fund on whose behalf the FIIs invests. Private companies, public companies, partnerships firms, pension funds, investment trust, and individuals are the following entities which are eligible to be registered as sub-accounts.
- A Foreign Institutional Investor is required to get itself registered and for this purpose, it is required to obtain a certificate from SEBI (SECURITY AND EXCHANGE BOARD OF INDIA) for dealing in securities. The certificate is granted by SEBI after it has taken into account the following criteria;
- An Applicant track record which includes its own record, financial soundness, competences, experience, general reputation, and fairness.
- The applicant must take permission to make foreign investment in India as a foreign institutional investor under the provision of foreign exchange regulation act, 1973 by the reserve bank of India.
- Applicant is regulated by a foreign regulated authority.
- Applicant must be a fit and proper person.
- Certificate which is granted to the applicant is in the interest of the growth of the securities market
- Applicant must be an international and multilateral organization or an agency or a foreign central bank.

CONDITIONS AND RESTRICTIONS WITH REGARD TO INVESTMENT

These are the following condition and restriction placed on the investment done by the foreign institutional investors.

- Securities in both primary and secondary markets places a debenture, shares, and warrant of companies either they are listed or unlisted or to be listed in the stock exchange.
- Scheme of units which is floated by domestic mutual funds including the trust o0f India either they are listed or unlisted
- Commercial paper
- Security receipt
- Securities dated by the government
- Derivatives trades on a recognized stock exchange

While giving the permission of investment, SEBI set prescribed conditions which may be compulsory with respect to the maximum amount which can be invested in the debt securities by foreign institutional investors on their account and on sub-account. An investment made in securities which are issued by the assets reconstruction companies or those companies who are under the Securitiny and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002.

Prohibition of FII

FIIs looking to invest in equity which is issued by an Assets reconstruction company and is not permitted under the SEBI rules, 1995. Foreign institutional investors are investing in any company which engaged in following activities:

- NIDHI COMPANY
- TRADING IN TRANSFERABLE DEVELOPMENT RIGHTS
- CONSTRUCTION OF BUSINESS
- REAL ESTATE BUSINESS
- AGRICULTURAL ACTIVITIES

Salient features of FII

- FIIs including mutual funds, pension funds, investment trust, banks, asset management companies, Nominee Company, incorporated/institutional portfolio manager or their power of attorney holder (providing discretionary and non-discretionary portfolio management services) would be welcomed to make investments under the new guidelines. Investment in all securities traded on the primary and secondary markets including the equity and other securities/instruments of companies which are listed/to be listed on the stock exchanges in India including the OTC Exchange of India is permitted.
- A foreign institutional investor is required to take initial permission from the SEBI for entering a market. A foreign institutional investor is having affiliated or subsidiary shall have to take separate registration with SEBI.
- A Foreign institutional Investor shall have to take various permissions under the Foreign Exchange Regulation Act, 1973 from the Reserve Bank of India because of the existence of foreign exchange controls in force. The registration shall be done under the single window approach.
- SEBI registration holds their registration for maximum five years along with the RBI general permission under the FERA, it is also valid for five years and both shall be renewed every after five periods in the future.
- The Foreign institutional investors will have the capacity to move, purchase and acknowledge capital gains on speculations on ventures made through the first corpus exchanged to India under the FERA consent. It might likewise buy in or take off rights offering of offers, contribute on all perceived stock trades through an assigned bank office and would have the capacity to designate a residential caretaker for the authority of the speculation.
- There is a limitation on the volume of investment and it should be minimum or maximum for the purpose of entry of foreign institutional investors in the primary market or secondary market and also lock in the period of outline for the objective of such investment made by the FIIs.

CONCLUSION

Foreign institutional investor's main aim is to make the proposal for investment in India which must register with the SEBI (SECURITY AND EXCHANGE BOARD OF INDIA) to participate in the market. Basically, these are the outside entities which are established in India. They are generally investing in Indian companies in stock and debenture under the rules and regulation of different companies.