

# The Effect of Foreign Institutional Investment on the Indian Stock Market: An overview

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## ABSTRACT

The effect of FII on the Indian stock market from 2000 to 2023 is the primary subject of this analytical study. This research seeks to answer the question, "What is the relationship between foreign institutional investment (FII) flows and the performance of the Indian stock market?" by using a mix of econometric models and statistical analysis. Reputable financial databases and regulatory authorities provided the data on FII flows, stock market indexes, and macroeconomic indicators. More foreign direct investment (FDI) often indicates higher market performance, according to the data, which demonstrate that FII has a positive and statistically significant effect on stock market returns. Additionally, the study identifies periods of high volatility where abrupt changes in FII flows lead to substantial fluctuations in the market indices. The results also suggest that FII is a critical factor influencing market liquidity and investor sentiment, contributing to the overall financial stability and growth of the Indian stock market.

**Keywords:** Foreign Institutional Investors (FII), Indian Stock Market, Nifty 50 Index

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## INTRODUCTION

### Foreign Institutional Investors (FII)

A foreign institutional investor (FII) is a person or organization that invests in a country other than its registered or headquarters nation. When talking about firms based outside of India that put money into the Indian financial markets, the term "foreign institutional investor" is probably used. China also uses the term in official contexts.

Mutual funds, pension funds, investment banks, insurance firms, and hedge funds are all examples of financial institutions that invest indirectly. FIIs can be significant sources of funding for developing economies, but many of these countries—including India—have imposed restrictions on the total amount of assets and the number of shares of stock that FIIs can acquire, especially in a single company.

This reduces the impact that FIIs have on specific businesses and the country's financial markets, as well as the possible harm that could result from FIIs withdrawing in large numbers during a crisis.

### Foreign Institutional Investors in Indian stock market:



**Fig.1 FII Investment in Indian Stock Market**

Foreign investments are regarded as essential for countries, particularly developing economies such as India's. The two main categories of foreign investors are foreign portfolio investments (FPIs) and foreign direct investments (FDIs). FDIs are financial investments made by an investor, business, or government from another nation to obtain a sizable ownership stake in a project or company that directly increases the output of goods and services in an economy. Non-resident FPI investments in Indian financial assets include shares, corporate, government, and convertible bonds as well as infrastructure securities. Some examples of FPIs are subaccounts, Foreign Institutional Investors (FIIs), and Qualified Foreign Investors (QFIs). Foreign institutional investors (FIIs) are large financial organisations including pension funds, mutual funds, and insurance firms.

### Regulations of FII in Indian Stock Market

The SEBI (Foreign Institutional Investors) Regulations, 1995 underwent a number of amendments in 1996–1997 in an effort to increase the diversity of foreign institutional investors and streamline the inflow of foreign portfolio investments. Facilitating debt securities investment through the FII route is another goal of the modifications. The following are the changes:

- Institutions may now apply to become FIIs if they have been running for at least five years and are enrolled with a regulatory body in their nation of creation or incorporation. Institutional funds, endowments, foundations, trusts, and organisations dedicated to philanthropy fall under this category.
- The maximum amount of equity that any one FII or sub-account of a FII may invest is 10% of the equity of that company, with a total investment cap of 24% for all FIIs, NRIs, and OCBs.
- For individual companies that have received shareholder approval, the 24 percent limit may be increased to 30 percent.
- FIIs are now able to purchase unlisted securities.
- Investment of FIIs' proprietary funds is permitted.
- FIIs are allowed to allocate all of their portfolios to debt securities as long as they receive special permission from SEBI. You may invest in government securities with a specific maturity date or corporate debt instruments that are listed or will be listed in the near future. The total cap on business borrowing from outside sources includes this investment.

Many FII endowment funds, proprietary funds, and 100% debt funds were finally registered as a result of these reforms. The report's Part II provides more information. SEBI and RBI established a coordination committee to streamline the FII registration procedure. At the close of the 1996–1997 fiscal year, neither SEBI nor RBI had any outstanding applications for FII registration.

Furthermore, international investors have been able to acquire Indian securities via Financial instruments issued by Indian issuers that are listed, traded, and settled overseas, include foreign currency convertible bonds, foreign currency bonds, and global depository receipts. Outside of the FII pathway, foreign investors may purchase Indian securities whether or not they are registered as FIIs. An investment's quantity and industry determine whether the RBI and the Foreign Investment Promotion Board (FIPB) need to approve it dependent upon the situation, or whether the RBI clearance is sufficient.

In addition, foreign financial services organizations are permitted to form joint ventures with Indian partners in the space of merchant banking, asset management, stock broking, and other financial services businesses. In order for foreign entities to participate in financial services, the FIPB must provide its permission. During 1996 and 1997, the FIPB issued regulations for non-banking financial services investment.

### List of top 10FII in India Stock Market:

1. **Singaporean Government:**For a few years now, the Singaporean government has been one of the biggest investors in India. It currently owns 43 stocks with a combined value of more than Rs. 121,000 Cr. in India.
2. **EU Growth Fund:**Another noteworthy investor is the EU Growth Fund. Having a net worth exceeding Rs 29,350 Cr, it owns six stocks. In India.
3. **Government Pension Global Fund:** The Government Pension Global Fund, based in Norway, has over Rs. 51,800 Cr invested in 65 stocks. within India.
4. Oppenheimer Funds
5. Abu Dhabi Investment Authority
6. Government Pension Fund Global
7. First State Investments
8. Aberdeen
9. Dodge & Cox International Stock Fund
10. Franklin Templeton Investments Funds

### List of top 10FII Holding Stocks in Nifty 50 Stocks:

1. Maruti Suzuki India Ltd.

2. UltraTech Cement Ltd.
3. Bajaj Auto Ltd.
4. Bajaj Finance Ltd.
5. Apollo Hospitals Enterprise Ltd.
6. Dr. Reddy's Laboratories Ltd.
7. Hero MotoCorp Ltd.
8. Britannia Industries Ltd.
9. LTI Mindtree Ltd.
10. Eicher Motors Ltd.

## REVIEW OF LITERATURE

**Dr. Syed Tabassum Sultana (2012)**-The impact of FII and FDI on the Indian stock market is the subject of this research. Taking market capitalization, stock indexes, and trading volumes into account, it investigates how these investments compare to the performance of the stock market. The research highlights the significant role FDI and FII play in driving market trends, indicating that increased foreign investment can lead to higher market stability and growth. The findings suggest that policies aimed at attracting foreign investments can positively impact the Indian stock market.

**Jatinder Loomba (2012)**-The article's focus is on the role that FIIs played in the turmoil of the Indian stock market. It analyses the patterns and behaviours of FIIs and their correlation with market fluctuations. The study finds that FII activities contribute to increased market volatility, highlighting the awareness of the Indian securities exchange to foreign investment movements. The research underscores the importance of monitoring FII flows to understand their impact on market stability and suggests that regulatory measures may be necessary to mitigate excessive volatility caused by such investments.

**Pooja Nagpal (2016)**-An Empirical Analysis of the Effects of FDI & FII on Indian Stock Market- Foreign institutional investment (FII) and foreign direct investment (FDI) have an impact on the Indian stock market, according to her research. Using empirical data, the research explores how these financial flows affect stock market indices and overall market performance. The findings suggest that both FDI and FII play significant roles in shaping market trends and can be indicators of economic health and investor confidence in India.

**Dr. Mayur Shah (2019)**-Dr. Mayur Shah is doing a dissertation on how foreign institutional investors have affected the stock market in India. If you want to know how foreign investment affects stock prices and market volatility, this article is for you. It looks at the association between FII inflows and market movements. The investigation discovered that FIIs significantly affect the Indian financial exchange, which influences development designs in the short and long term.

**P. K. Mishral (2009)**-The position of FIIs in the Indian stock market is examined in the article by P. K. Mishral. It investigates the extent to which FII investments affect market dynamics, liquidity, and investor behavior. Based on their potential to increase market liquidity and provide growth-funding capital, FIIs assume a fundamental part in the turn of events and stability of India's capital market, according to the report. Additionally, it underscores the potential risks associated with high dependency on FII inflows, such as market volatility and susceptibility to global financial trends.

**Ruchika Gahlot (2018)**-An analytical study on effect of FIIs & DIIs on Indian stock market- This study, published in the Journal of Transnational Management, investigates the impact of Foreign Institutional Investors (FIIs) and Domestic Institutional Investors (DIIs) on the Indian stock market. Gahlot uses statistical analyses to explore how these institutional investments influence market volatility and overall market performance. The findings suggest that both FIIs and DIIs play significant roles in shaping market dynamics, with their investment behaviours affecting market liquidity and investor sentiment. The study also highlights the contrasting effects of FIIs and DIIs, providing insights into how these entities interact with market conditions.

**Abhijeet Chandra (2012)**-The study employs econometric models to analyse the bidirectional influences between FII trading behaviour and market performance. The results indicate that FII trading activities not only respond to stock market movements but also have a predictive effect on future market returns. This bidirectional causality suggests a feedback loop where FIIs both influence and are influenced by market trends.

**Harsh Vardhan (2016)**-Using VAR models, this essay explores how FIIs have affected the Indian stock market. A publication of the Journal of Emerging Market Finance, we find it. Research by Vardhan delves into the multifaceted connection between foreign institutional investors'(FIIs') streams and stock market lists, offering an extensive examination of how FII investments impact market volatility and returns. Report discoveries demonstrate that FIIs assume a significant part in the development and dependability of the stock market via their investment techniques.

The use of VAR models allows for a nuanced understanding of the temporal relationships and the endogenous effects within the market.

**K.V. Bhanu Murthy (2013)-Is the Indian Stock Market Truly Influenced by Foreign Institutional Investors?-** A focus of this piece is the impact that FIIs, or foreign institutional investors, have had on the stock market in India. To determine if FIIs are the driving factors behind market swings, Murthy studies the relationship between's FII capital streams and stock market records. The study utilizes various statistical tools to determine causality and the extent of influence that FIIs exert on market volatility, liquidity, and overall performance. Although foreign institutional investors (FIIs) certainly have an effect, the results show that this is not the only factor influencing market dynamics. Other factors, such as domestic institutional investors and macroeconomic indicators, also play crucial roles (Manage.gov.in).

**Shrikanth, Maram and Kishore Braj (2012)-Net FII Flows into India: A Cause-and-Effect Study-** This research reviews the connection between FDI inflow and the Indian stock market and was published in the ASCI Journal of Management. Shrikanth and Braj employ econometric models to explore how FII inflows affect market liquidity, stock prices, and the cost of equity capital. They find that FII flows significantly enhance market liquidity and contribute to lowering the cost of capital for Indian companies. However, they also caution that these flows can introduce volatility, particularly during periods of economic or political instability. The study concludes that while FIIs assume a vital part in the Indian capital market, their influence is moderated by other domestic and international factors.

**OBJECTIVES OF THE STUDY**

The following three goals constitute the primary scope of this research:

- ✓ To provide a definition, an explanation, and context for the significance of foreign institutional investment in relation to the Indian stock market.
- ✓ To assess FII inflows and outflows in India over a given time period in terms of volume, trends, and patterns.
- ✓ To provide insights into how policymakers can enhance the positive impacts of FII while minimizing potential negative effects.

**DATA & METHODOLOGY**

The secondary data used in this study is entirely sourced from websites, financial platforms, periodicals, and other online sources.

**ANALYSIS & INTERPRETATION**

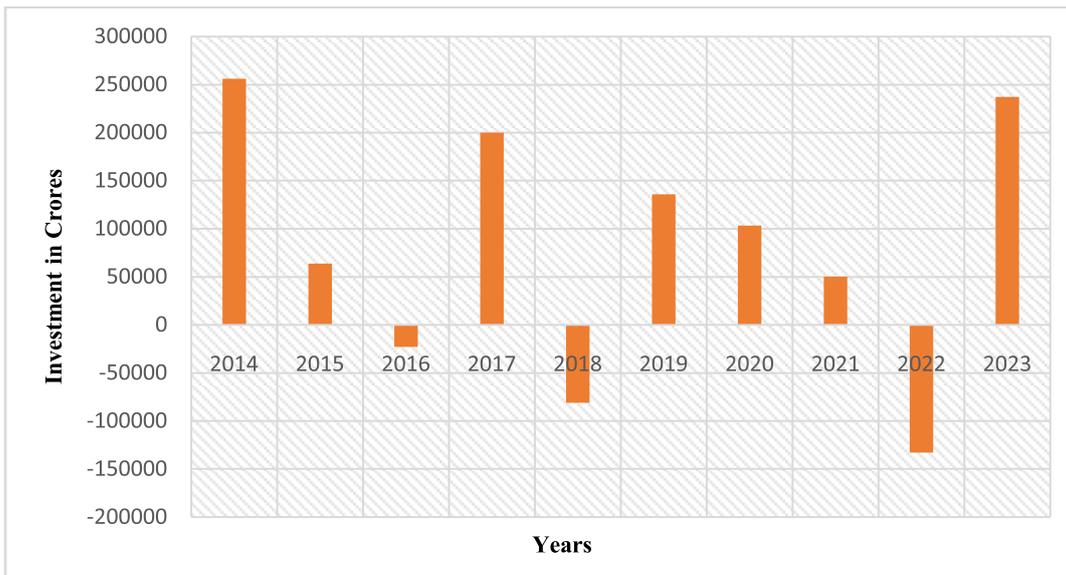
**Table 1.1** shows the FII investment in Last ten years from 2014 to 2023 by analysing the below table clearly shows that year wise FII investment in the years 2016, 2018, 2022 was negative and in the all-remaining years were positive and the highest investment took place in the year 2014 i.e., Rs.2,56,211.85 Crores.

**Table 1.1 FII Investment in Last Ten Years**

<b>Years</b>	<b>Total Investment*Amount (INR Crores)</b>
2014	256211.85
2015	63662.21
2016	-23079.12
2017	200048.12
2018	-80917.23
2019	135993.59
2020	103158.04
2021	50088.66
2022	-132815.22
2023	237061.27

Source:www.cdslindia.com

\*Total Investment = Equity + Debt + Debt-VRR + Hybrid



**Fig.1.1 FII Total Investment Amount**

**Table 1.2** Compares FII Investment and Nifty 50 Index Over the Past Ten Years. Examining the table below makes it evident that, in the year from 2014 to 2015, FII investment decreased while the Nifty 50 Index decreased as well. In 2015 to 2016, FII investment turned negative while the Nifty 50 Index did not change significantly. Finally, in 2022 to 2023, FII investment increased while the Nifty 50 Index increased significantly. There is no denying the substantial influence that FII investment has on the Indian stock market. Whenever FII investment declines and turns negative, the Nifty 50 Index likewise experiences a negative reaction and stays unchanged.

**Table 1.2 FII Investment and Nifty 50 Index Comparison in Last Ten Years**

Years	Total Investment Amount (INR Crore)	Nifty 50 Index at the Year End	Percentage (%) Change
2014	256211.85	8,282.70	31.30%
2015	63662.21	7,946.35	-4.00%
2016	-23079.12	8,185.80	2.88%
2017	200048.12	10,530.70	28.60%
2018	-80917.23	10,862.55	3.15%
2019	135993.59	12,168.45	12%
2020	103158.04	13,981.75	14.90%
2021	50088.66	17,354.05	24.12%
2022	-132815.22	18,105.30	4.32%
2023	237061.27	21,731.40	20%

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

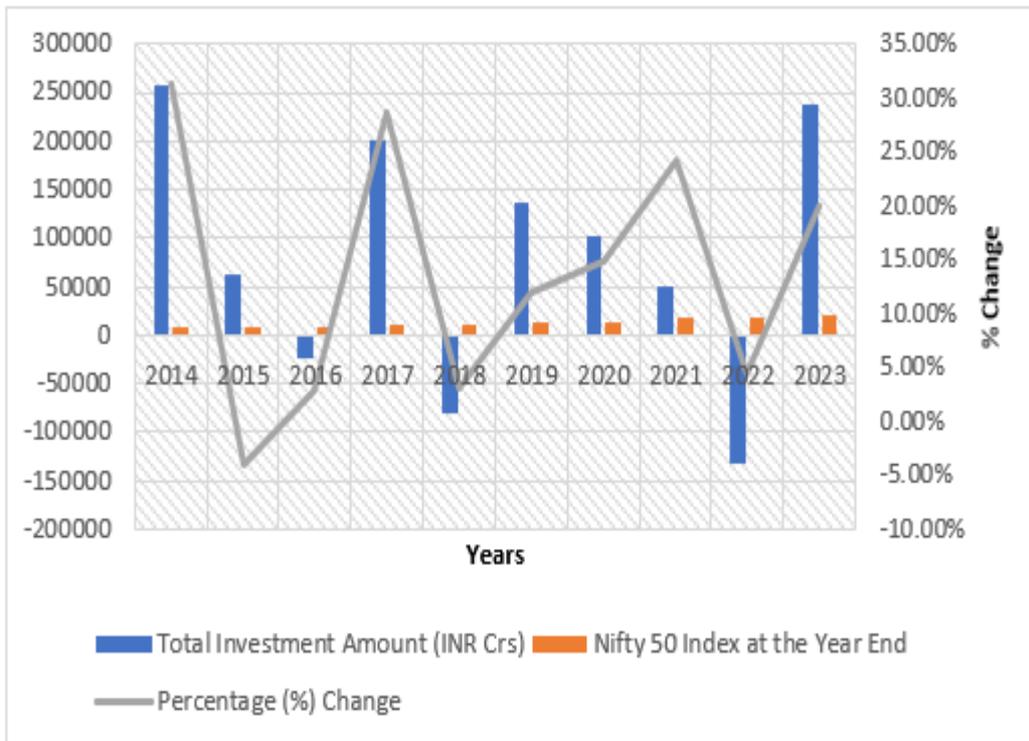


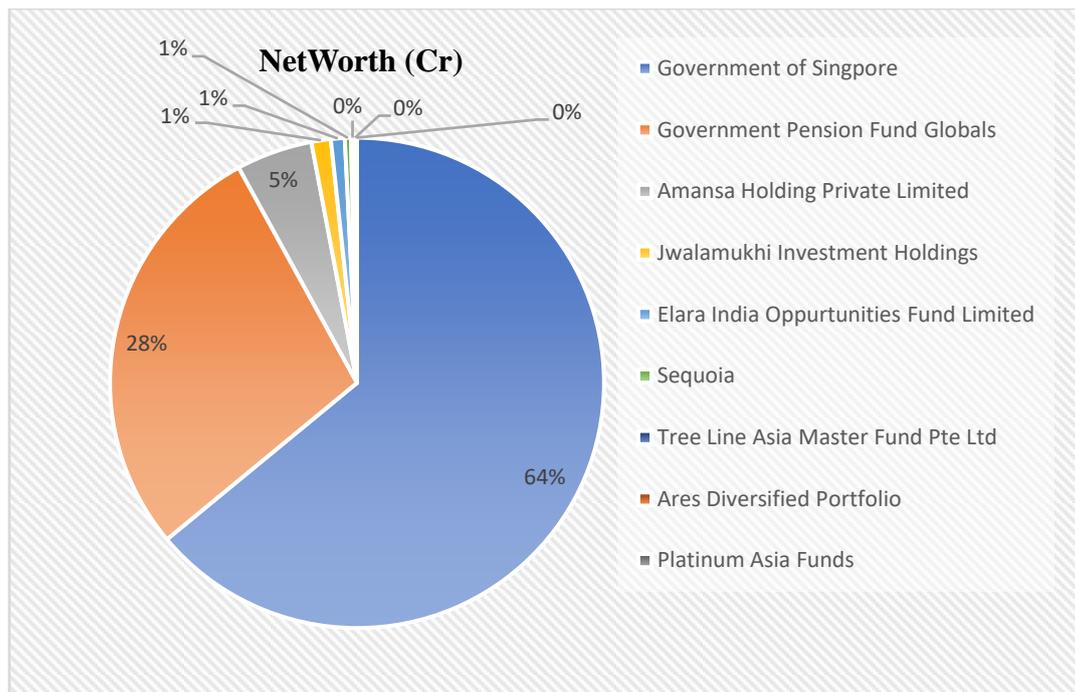
Fig. 1.2 FII Investment and Nifty 50 Index Comparison in Last Ten Years

Top FII Holding in Indian Stock Market:

Table 1.3 Top FII Holding Network  
 \*As on Quarter Mar-2024

FII Name	Networth (Cr)
Government of Singapore	2,70,680
Government Pension Fund Global	1,18,796
Amansa Holding Private Limited	21,072
Jwalamukhi Investment Holdings	5,349
Elara India Opportunities Fund Limited	3,845
Sequoia	1,687
Tree Line Asia Master Fund Pte Ltd	871
Ares Diversified Portfolio	504
Platinum Asia Funds	278

Source: www.moneycontrol.com



**Fig.1.3 Top FII Holding Networth in Indian Stock Market**

### FINDINGS

- The Indian stock market is significantly impacted by foreign institutional investors (FIIs). The way they trade has an impact on stock prices and market trends. The connection between FII net venture and stock market returns in India provides support for the hypothesis of bidirectional causation, according to which FIIs would rather follow market performance than set their own.
- Market volatility is a result of FII activity. FIIs' large-scale purchases or sales may cause brief changes in stock prices. Herding behaviour among FIIs, where they frequently make similar investment choices based on market trends, is partially to blame for this increased volatility.
- FIIs are essential to the Indian stock market's ability to maintain liquidity. Their investments contribute to increased market liquidity and depth, which facilitates the buying and selling of securities by other investors without materially impacting prices.
- International financial institutions continue to back the stock market's long-term growth despite its short-term instability. Over time, the market benefits from their investments as they are linked to enhancements in corporate governance and market efficiency.

### SUGGESTIONS

- ✓ To entice and hold onto FII investments, the Indian government and regulatory agencies ought to establish a stable and welcoming atmosphere for investors. This include preserving macroeconomic stability, guaranteeing open and understandable regulatory environments, and offering sufficient safeguards for investors.
- ✓ To understand how FII operations impact market dynamics, it is essential to monitor their actions closely. The market can be stabilized by putting policies in place to control excessive volatility brought on by erratic FII capital inflows or outflows.
- ✓ Promoting FII investment diversification across various industries and securities can help to lower the risk of market concentration and the possibility of significant market disruptions.
- ✓ Enhancing the efficiency and allure of the Indian stock market for international investors can be achieved by improving market infrastructure, including trading platforms and settlement systems.

### CONCLUSION

In general, the stock market does better when FII is involved. The volatility and liquidity of the market are greatly impacted by the inflow and outflow of foreign institutional investments. Increased market stability and liquidity, which promote smoother transactions and price discovery, are typically correlated with higher FII inflows. High FII inflow periods are typically linked to bullish market trends, while outflow periods are typically associated with bearish conditions.

In order to attract and retain international investment, the report stresses the need of maintaining a favourable investment environment. For FII inflows to continue, stable economic policies, clear regulatory frameworks, and an open market are essential. FII carries some risks but can also improve market performance. Large-scale, abrupt withdrawals by foreign investors have the potential to cause severe market declines, underscoring the importance of effective risk management techniques.

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