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ROLE OF FDI & FII IN ECONOMIC GROWTH

N.Pavani

Asst.Professor, Gayathri College for PG courses, Munsabpeta. 532401.
SRIKAKULAM, ANDHRAPRADESH.

Abstract

Foreign Direct Investment (FDI) and Foreign Institutional investment (FII) plays a vital role in accelerating economic growth of any economy. The Foreign investment can be made either in the listed companies through financial companies like FDI and FII. Foreign Direct investment increases the domestic investments by increasing economic activities and other capital formation as well as new technology adaption. It makes domestic market more competitive.FII leads the domestic investments by increasing capital inflows through secondary market. FDI plays more important role than FII in process at any developing country/Economy.FDI provides not only inflow of foreign funds and investments but also transfer of advanced technology, skills and creating employment. Both of (FDI & FII) foreign investments provide an impetus for economic growth & development. The present paper tries to do a comparative and comprehensive analysis of FDI &. FII and contribution towards economic growth. For the data of the time series its applied on time period from 2016 to 2018
Keywords: - FDI and FII

Introduction of FDI and FII

Foreign investment refers to investments made by the residents of a country in the financial assets and production processes of another country. The effect of foreign investment, however, varies from country to country. It can affect the factor productivity of the recipient country and can also affect the balance of payments. Foreign investment provides a channel through which countries can gain access to foreign capital.

It can come in two forms: Foreign direct investment (FDI) and Foreign institutional investment (FII). Foreign direct investment involves in direct production activities and is also of a medium-to long-term nature. But foreign institutional investment is a short-term investment, mostly in the financial markets.

FII, given its short-term nature, can have bidirectional causation with the returns of other domestic financial markets such as money markets, stock markets, and foreign exchange markets. Hence, understanding the determinants of FII is very important for any emerging economy as FII exerts a larger impact on the domestic financial markets in the short run and a real impact in the long run. India, being a capital scarce country, has taken many measures to attract foreign investment since the beginning of reforms in 1991

SCOPE AND NEED OF STUDY:

Scope of the study is very broader and covers both the stock indices and its comparison with foreign institutional investments. But, study is only going to cover foreign investments in form of equity. The time period is limited from January 2016 to December 2018 as it will give exact impact in both the bullish and bearish trend.

The study will provide a very clear picture of the impact of foreign institutional investors on Indian economy. It will also describe the market trends due to FDI and FII inflow and outflow.

The study would be helpful for further descriptive studies on the ideas that will be explored. Moreover, it would be beneficial to gain knowledge regarding foreign institutional investments, their process of registration and their impact on economic growth of developing countries

OBJECTIVES OF THE STUDY:

- To study the scope and trading mechanism of Foreign Institutional investors in an economy
- To analyze the impact of FIIs equity investment on specific industrial sector (FMCG, Consumer Durables, Auto, Banking, Real Estate) indices.

Importance of FDI & FII

- To financial transfers in foreign exchange. To import production technology.
- To developer management skills.
- To import of physical resources like Machinery, Tools and equipment. To improve worldwide contracts.
- To develop training and research programs. To increase trade channels

Foreign direct investment (FDI)

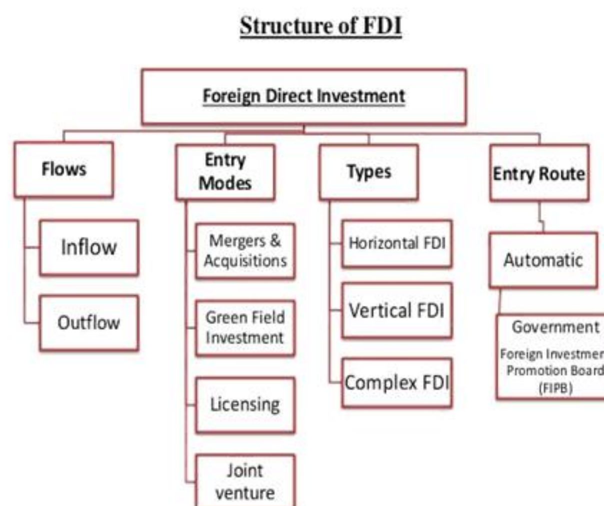
Foreign direct investment (FDI) is made into a business or a sector by an individual or a company from another country. It is different from portfolio investment, which is made more indirectly into another country's economy by using financial instruments, such as bonds and stocks.

The Organization of Economic Cooperation and Development (OECD) define control as owning 10 per cent or more of the business. Businesses that make foreign direct investments are often called multinational corporations (MNCs) or multinational enterprises (MNEs).

According to the IMF and OECD definitions, direct investment reflects the aim of obtaining a lasting interest by a resident entity of one economy (direct investor) in an enterprise that is resident in another economy (the direct investment enterprise). The "lasting interest" implies the existence of a long-term relationship between the direct investor and the direct investment enterprise and a significant degree of influence on the management of the latter.

There are various levels and forms of foreign direct investment, depending on the type of companies involved and the reasons for investment. A foreign direct investor might purchase a company in the target country by means of a merger or acquisition, setting up a new venture or expanding the operations of an existing one. Other forms of FDI include the acquisition of shares in an associated enterprise, the incorporation of a wholly owned company or subsidiary and participation in an equity joint venture across international boundaries.

Structure of FDI



Advantages of FDI

Economic Development Stimulation. Competitive advantage and innovations. Employment and Economic Boost. . Development of Human Capital Resources. Tax Incentives.
Reduced Disparity Between Revenues and Costs. Increased Productivity.
Inflow of equipment and technology

Disadvantages of FDI

Hindrance to Domestic Investment. Risk from Political Changes.
Negative Influence on Exchange Rates.
Loss of control
Conflicts of codes and laws.
Very risky or economically non-viable.
Negative Impact on the Country's Investment.

Foreign Institutional Investors (FII)

Foreign institutional investors (FIIs) are those institutional investors which invest in the assets belonging to a different country other than that where these organizations are based.

Foreign institutional investors play a very important role in any economy. These are the big companies such as investment banks, mutual funds etc, who invest considerable amount of money in the Indian markets. With the buying of securities by these big players, markets trend to move upward and vice-versa. They exert strong influence on the total inflows coming into the economy.

Market regulator SEBI has over 1450 foreign institutional investors registered with it. The FIIs are considered as both a trigger and a catalyst for the market performance by encouraging investment from all classes of investors which further leads to growth in financial market trends under a self-organized system.

Also See: Domestic Institutional Investors, SEBI, Mutual Funds, Hedge Funds, Banks, Insurance Companies, BSE, NSE, Capital Market Segment, Capital Inflows

Advantages of FII

Enhanced Flow of Capital of the host country Managing Uncertainty and Controlling Risks
Improved Corporate Governance and overcome problems of principal-agent. Economic Development.

Disadvantages of FII

Potential Capital Outflow. Problem of Inflation.
Adverse Impact on Exports. Problems for small Investors.

Impact of FDI and FII on Developing Countries

Many developing countries do not have the necessary resources at their disposal to develop some sectors and hence, they permit foreign capital to invest in these sectors. Of course, they also ensure that sectors like defense and other sectors that have national security implications are kept off the list of sectors in which foreign direct investment (FDI) is allowed. For many countries, opening up of their economies results in benefits since they need the dollars as well as be-

cause they might not have the expertise to commence productive activities in these sectors. Finally, foreign direct investment can be used to pay for expensive imports and encourage exports as well. After all, every developing country (except those with large oil reserves) needs to pay for its oil imports in dollars and hence FDI helps to earn precious dollars.

A significant portion of corporate sector's securities are held by Foreign Institutional Investors (FII), such as pension funds, mutual funds and insurance companies. These investors are often viewed as sophisticated investors as these institutional investors are better-informed and better equipped to process information than individual investors

The impact FIIs flows on domestic stock market is important from governments well as investor point of view, for example, does the opening up of the market for FII increase speculation in the market and thus make the market more volatile and more vulnerable to foreign shocks The Impact of FII in equity investment behavior in stock Market

Financial liberalization increases the efficiency of financial market and permission of FIIs equity investment are an important example of financial liberalization. Apart from net investment of FII's the purchase and sale behavior of FIIs were also analyzed in the study. The researcher has studied and analyzed FII flows and examined if the overall experience has been stabilizing or destabilizing for the Indian capital market.

Difference between FDI and FII

Both FDI and FII is related to investment in a foreign country. FDI or Foreign Direct Investment is an investment that a parent company makes in a foreign country. On the contrary, FII or Foreign Institutional Investor is an investment made by an investor in the markets of a foreign nation.

In FII, the companies only need to get registered in the stock exchange to make investments. But FDI is quite different from it as they invest in a foreign nation.

The Foreign Institutional Investor is also known as hot money as the investors have the liberty to sell it and take it back. But in Foreign Direct Investment, this is not possible. In simple words, FII can enter the stock market easily and also withdraw from it easily. But FDI cannot enter and exit that easily. This difference is what makes nations to choose FDI's more than then FIIs.

FDI is more preferred to the FII as they are considered to be the most beneficial kind of foreign investment for the whole economy.

Foreign Direct Investment only targets a specific enterprise. It aims to increase the enterprises capacity or productivity or change its management control. In an FDI, the capital inflow is translated into additional production. The FII investment flows only into the secondary market. It helps in increasing capital availability in general rather than enhancing the capital of a specific enterprise.

The Foreign Direct Investment is considered to be more stable than Foreign Institutional Investor. FDI not only brings in capital but also helps in good governance practices and better management skills and even technology transfer. Though the Foreign Institutional Investor helps in promoting good governance and improving accounting, it does not come out with any other benefits of the FDI.

While the FDI flows into the primary market, the FII flows into secondary market. While FIIs are short-term investments, the FDI's are long term.

Countries with Most FDI In 2018

Even as the world saw improving GDP numbers and growth in trade, global flows of foreign direct investment (FDI) fell by 16per cent in 2017 to an estimated $1.52 trillion. They stood at $1.81 trillion in 2016. "FDI recovery continues to be on a bumpy road" said UNCTAD Secretary-General Mukhisa Kituyi. "While FDI in developing countries remained at a level similar to the previous year, more investment in sectors that can contribute to the Sustainable Development Goals is still badly needed. Promoting FDI for sustainable development remains a challenge."

Decrease in FDI flows to developed economies was a major reason for decline in overall global numbers. Both Europe and North America saw a decline in inflows at -27per cent and -33per cent respectively. FDI to developing economies remained stable at $653 billion and saw a 2per cent increase year-on-year. Investment flows to Latin America, the Caribbean and developing Asia rose marginally. FDI remained flat for Africa.

Despite the decrease, the United States received the lion's share of global FDI at $311 billion followed by China that saw record inflows at $144 billion.

Take a look at the graphic below for the top 10 countries that received the most FDI in 2017 and 2018

Foreign Direct Investment By Country

TABLE 1:

Country	(Rs in crores)	
Argentina	243.74	18-Aug
Australia	60499	17-Dec
Brazil	10607	18-Aug
Canada	11674	18-Jun
China	917.7	18-Sep
France	3013	18-Aug
Germany	2480	18-Jul
India	1898	18-Aug
Indonesia	95.7	18-Jun

Italy	1848	18-Aug
Japan	13545	18-Aug
Mexico	6726.9	18-Jun
Netherlands	-24697	18-Jun
Russia	2583	18-Jun
Saudi Arabia	882	18-Jun
Singapore	25531.7	18-Jun
South Africa	1863	18-Jun
South Korea	3448981	18-Sep
Spain	3789	18-Jul

Here, we present the companies with highest Foreign Institutional Investors (FIIs) holding in BSE companies.
TABLE 2:

Company Name	Industry	FII (%)
Housing Development Finance Corporation	Finance	78.03
Shriram Transport Finance Company	Finance	52.34
Zee Entertainment Enterprises	Entertainment	50.84
IDFC	Finance	47.62
Axis Bank	Finance	47.6
UPL	Chemicals	46.53
YES Bank	Finance	46.3
IndusInd Bank	Finance	43.2
Infosys	Computers	42.67
Housing Development & Infrastructure	Construction	42.54

Conclusion

Investing into another country's economy, buying into a foreign company or otherwise expanding your business abroad can be extremely financially rewarding and might provide you with the boost needed to jump to a new level of success. However, foreign direct investment (FDI) and Foreign Institutional Investment (FII) also carries risks, and it is highly important for you to evaluate the economic climate thoroughly before doing it. Also, it is essential to hire a financial expert who is accustomed to working internationally, as he can give you a clear view of the prevailing economic landscape in target country.

Summary

FDI is an investment that a parent company makes in a foreign country. On the contrary, FII is an investment made by an investor in the markets of a foreign nation.
Foreign Direct Investment targets a specific enterprise. The FII increasing capital availability in general.
The Foreign Direct Investment is considered to be more stable than Foreign Institutional Investor
FDI and FII being a long term investment has also improved the balance of payment and employment generation

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