IJBARR
E- ISSN -2347-856X
ISSN -2348-0653

FII, MUTUAL FUND AND SOME MACRO ECONOMIC VARIABLES: IS THERE ANY RELATIONSHIP IN PRESENT INDIAN CONTEXT?

Ruma Dey* **Sabyasachi Bose****

**Assist. Professor, Department of Commerce, Mathabhanga College, Mathabhanga, Coochbehar, W.B.*
***Lecturer-in-Commerce (PTT) Department of Commerce. Siliguri College of Commerce, Siliguri, Darjeeling, W.B.*

Abstract
The cross-border movements of capital and its impact on several aspects of national capital market has been a serious research topic for several scholars for last few decades. FIIs have invested a net of US$ 43.5 billion in 2014-2015 – expected to be their highest in any fiscal year. FIIs net investments in Indian equities and debt are set to touch a record in 2015-2016 financial years, backed by expectations of an economic recovery, falling interest rates and improving earnings outlook. Domestic mutual funds, on the other hand, are expected to play the all-important role of channelizing domestic savings into the financial market. This role takes on a far greater significance in developing markets like India where a vast majority of investors are not yet comfortable with investing directly in the stock market. This study has examined the dynamic interaction between institutional investment flows of two most important classes of institutional investors operating in Indian stock market, namely, Mutual Funds and FIIs in the context of different macroeconomic variables. The findings of this research suggest that long term developmental policies for economy should not be based upon inflow of FIIs. Mutual funds should invest more in equity in the stock market and there is much scope to propel the fund channelizing policy making towards Indian debt market. The policy makers may concentrate on this issue.

Key Words: FII, Mutual Funds, Macroeconomic Variables, Tourist Investors, Financial Liberalization, Fund Channelization.

INTRODUCTION

The mainstream argument that the influx of Foreign Institutional Investment can fillip the stock market and thus, economic development of the LDCs, including India, seem to be lacking acclamation. On 14th September 1992, FIIs and Overseas Corporate Bodies (OCBs) were permitted to invest in financial instruments including Mutual Funds and presently 1742 registered FIIs are operating in Indian stock market till December, 2013 and have pumped in over Rs.1 lakh crore into Indian equities over the course of the year with a tag of 'hot-money'. FIIs have invested a net of US$ 43.5 billion in 2014-2015 – expected to be their highest in any fiscal year. FIIs net investments in Indian equities and debt are set to touch a record in 2015-2016 financial year, backed by expectations of an economic recovery, falling interest rates and improving earnings outlook. Irrespective of nature of economy the macroeconomic variables are supposed to get affected by the inflow of fund through tourist investors (FIIs). A well-recognized stock market of any country has considered being an important part for the development of economy (Bohra & Dutt, 2011). Economic growth is a function of capital formation in respect of factors of production. The concept of financial liberalisation has augmented global financial market integration to facilitate 'cross-country cross-industry' diversification of funds to reduce the portfolio risk with emphasis on systematic risk minimization (Roy & Ray, 2011). Thus, Foreign Portfolio Investment controlled by Foreign Institutional Investors has been playing a dynamic role to influence capital market volatility, foreign exchange rates and the money market interest rates especially in developing countries since late 1980s when they started liberalising their financial sectors. In India, since 1992, the national capital market was opened for the FIIs and now they can invest their own funds as well as invest on behalf of their overseas clients registered as such with Securities Exchange Board of India (SEBI).

Foreign Institutional Investment is defined as individual or institution organized outside the country for the purpose of making investments into the internationally diversified portfolio rather than to acquire control over foreign companies. The major players behind the Foreign Institutional Investments are overseas pension funds, mutual funds, investment trust, asset management company, bank, institutional portfolio manager, university funds, endowments, foundations, charitable trusts, charitable societies, a trustee or power of attorney holder incorporated or established outside the country proposing to make proprietary investments or investments on behalf of a broad-based fund. On the other hand, According to SEBI (Mutual Funds) Regulation 1996, Mutual Funds means "fund established in the form of a trust to raise money through the sale of units to the public or a section of public under one or more schemes for investing in securities including money market instruments or gold or gold related instruments or real estate assets". A special type of institution that act as an investment conduit is called "mutual fund''. It is essential mechanism of pooling together the savings of a large number of investors for collective investment with the objective of attractive yield appreciation of their investment. Mutual Funds are non-depository financial intermediaries. Mutual Funds are the mobilisers of savings particulars of the small and household sectors for investment in the stock and money market. The researcher in this project has tried to explore the dynamics of relationship between

 IJBARR
E- ISSN -2347-856X
ISSN -2348-0653

investment flows to the stock market from two major categories of institutional investor in Indian economy, namely, Mutual Funds and Foreign Institutional Investors in the context of few selected macroeconomic variables.

Advantages and Disadvantages of FII

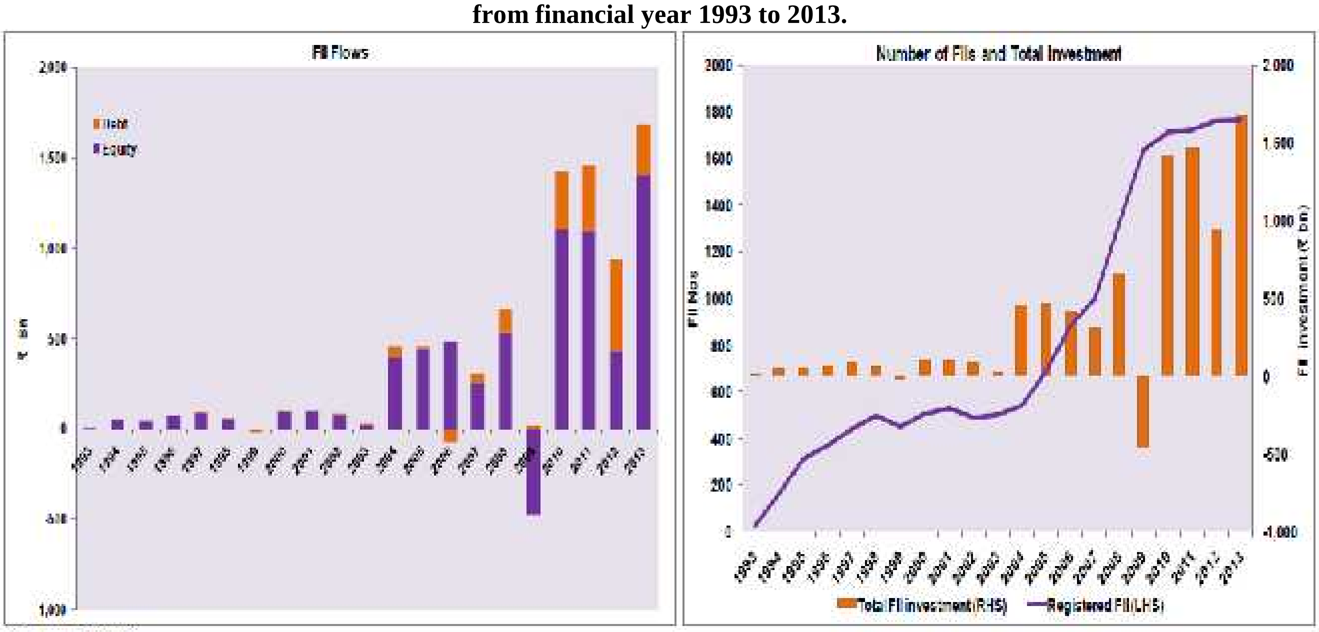
The comparative advantage of return maximization from investment and a variety of incentives offered by competing economies have fuelled the 'hot-money' activities all over the globe. Advocators of free movement of capital argue that Foreign Portfolio Investment (FPI) tends to increase the liquidity and the efficiency of local markets in short-run and benefit the economies of the recipients' countries by reducing the cost of capital. The efficacy of foreign funds makes raising of capital conducive for venture-companies and new or existing companies who are bearing comparatively higher risks. In the long-run, the quality and infrastructure of the financial institutions and markets of the recipient economies are claimed to be enhanced by the competitiveness induced by the FPIs. Beside, good corporate governance, the level of accounting standards and practices also get closer to international standards. Though the tag of 'fair-weather friend' is always attached with these funds, the controlled and directed utilization of funds from FIIs may result in economic and financial benefits for the host countries (Ray et al. 2013).

The multi-dimensional effects of FPI on development have not been adequately delved in many emerging markets and their multi facet impact on economic development is not explored sufficiently. Some researchers have argued that noisy features of equity market like, speculations, volatility clustering, etc. are the aftermath of FPI flows that are willing to make 'quick money'. At the same time, the threat of take over through secondary equity market creates non-favourable environments in the economy of emerging and developing countries. Scholars also observed that the influx of FII has failed to motivate equity markets like India and do not lead to economic development. The 'Mexico-Style' trading behaviour of FPI's, that is, withdrawal of partial or entire capital at the slightest hint of weakness of the economy or the political instability may gift a sudden calamity to the equity market, foreign exchange market, money market, balance of payment etc. and may converge to a point of economic crisis. Irrespective of economic or financial status, this crisis of one country may spread to other countries (Pal, 1998, Chakraborti, 2001, Ray et al., 2013).

FDI and FII

While removing the prevailing ambiguity on what is FDI and what is FII, Mr. P. Chidambaram, the former Finance Minister of the Government of Indian, in his budget speech of the year 2013-2014 declared that foreign investors with less than 10 per cent stake in a particular stock will be considered as FII and more than 10 per cent stake as FDI. FDI entities are considered promoter group shareholders in companies and FIIs as public shareholders. FDIs are allowed to conduct private transactions while FIIs are not. FDIs attract up to 40 per cent tax and are bound by lock-in-periods in their investments as promoters. On the other hand, FIIs attract up to 30 per cent tax.

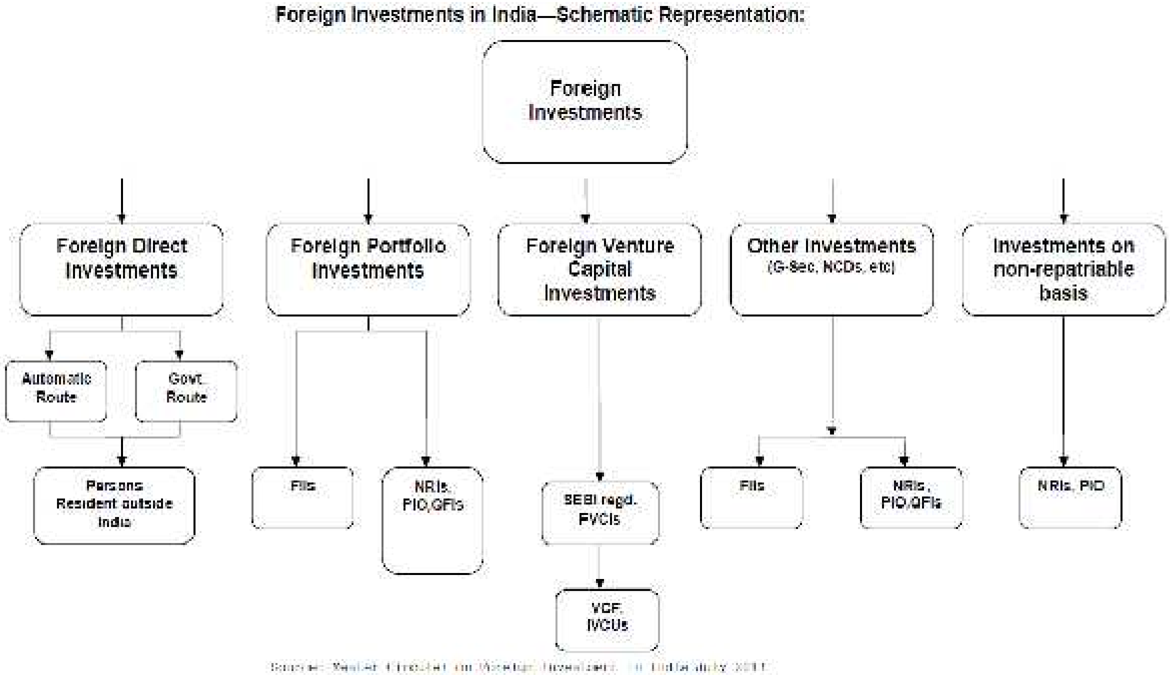
Charts below shows FII flows in equity and debt and registered FII numbers with total investment (equity +debt) from financial year 1993 to 2013.



Source: SEBI

IJBARR
E- ISSN -2347-856X
ISSN -2348-0653

INVESTMENT PATTERN OF FIIs IN INDIAN STOCK MARKET



FDIs flow into the primary market on a long-term basis and aim at increasing enterprise productivity or change its management control. Whereas FIIs flow only into the secondary market on a short-term basis and results in increase in capital availability in general rather than enhancing the capital of a specific enterprise.

REVIEW OF LITERATURE

Loomba (2012) has used ‘Pearson Correlation’ to understand the dynamics of the trading behaviour of FIIs and its effect on the Indian equity market. The study is based on daily data. BSE Sensex and FII activity over a period of 10 years spanning from 1st January 2001 to 31st December 2011 is observed. He found a significant positive correlation between FII activity and effects on Indian Capital Market and concluded that the movements in the Indian Capital Market are fairly explained by the FII net inflows. Covering the same time period and almost same data set, Walia et al. (2012), Jain et al. (2012), examined the similar issues and reported the similar observations like Loomba (2012). Unit-root test, co-integration and long-run Granger causality test (Toda and Yamamoto, 1995) are used by Md. Ali (2011) to test the causal relationships between the Dhaka Stock Exchange (DSE) Index and the thirteen macroeconomic variables, viz., consumer price index, deposit interest rate, foreign exchange rate, export payment, gross domestic product, investment, industrial production index, lending interest rate, broad money supply, national income deflator, foreign remittances and total domestic credit. He has used monthly data for the period 1987 to 2010. The major findings are that DSI, in any way do not granger cause CPI, deposit interest rate, export receipt, GDP, investment, industrial production index, lending interest rate and national income deflator. But unidirectional causality is found from DSI to broad money supply and total domestic credit. In addition bi-directional causality is also identified from DSI to exchange rate, import payment and foreign remittances. Suchismita Bose has done a research on mutual fund investment, foreign institutional investor investment and stock market return in India in the year 2012 to see how FII impacts the mutual fund investment and stock market return. The study reveals that FII investment patterns are consistently significant as the causal variable for changes in mutual fund flows, with a significant negative relationship between FIIs and mutual funds.

OBJECTIVE OF THE STUDY

The key objective of this study is to investigate whether any relationship exists between FII flow, Mutual Fund investments and Macroeconomic variables’ performance in India so that policy makers and investors in capital market can get benefitted. With respect to the vastness of macroeconomic variables, the present study has been kept limited to cover GDP, Total Investment, Unemployment Rate, Imports, Exports, SENSEX, Weighted Average Call Money Rates, Inflation Average Consumer Price, and Gross Domestic Saving. In order to give better picture of the role of FIIs in Indian growth, the study has focused on relationship between FII and Macroeconomic variables and relationship between FII and Mutual Fund investment patterns respectively.

RESEARCH METHODOLOGY

To achieve objectives, the study used monthly data for the time period 2010-2011 to 2014-2015 financial years for FII and Mutual Fund investments series and over the period January 2001 to December 2010 for FII and Macroeconomic variables, depending on availability of data from various authentic sources. Data for selected macroeconomic variables were gathered from SEBI website, BSE website, NSEI website, The Economic Times and The Money Control website. There can be both short-run and long-run relationships between financial time series. Karl Pearson's coefficient of correlation ($-1 < p < 1$) and Regression equations are used for examining short-run co-movements and collinearity among the variables. However, the research is more descriptive and analytical in nature based on the assumption that historical data is identically and independently distributed.

FINDINGS

The Net Investments by FII (X) and GDP (Y) of India during 2001-2010 are positively related to each other. However, the degree of relationship is insignificant. Thus, it may be said that the GDP of India and FII flows during the stipulated time period were merely independent to each other (Table-1). The Net Investments by FII (X) and Inflation at Average Consumer Price (Y) of India during 2001-2010 are positively related to each other. However, the degree of relationship is not significant. Thus, the Inflation at Average Consumer Price of India and FII flows during the given time period may not be dependent to each other. The research has revealed that almost same relationship exist between FII (X) and Total Investment (Y), Unemployment of India (Y), Weighted Average Call Money Rates of India (Y), Gross Domestic Savings of India (Y), Exports of India(Y), Imports of India (Y) and Sensex (Y). Though the data time period in some cases are different, relationship between FII and the selected variable has not yield a different result.

Table 1: showing relationship between FII and Macroeconomic variables

Macroeconomic Variables	**Karl Pearson's coefficient of correlation (r) with FII**	**Result (Significant/Insignificant and Positive/Negative)**
GDP	0.00187	Insignificant Positive Relation
Inflation	0.029	Insignificant Positive Relation
Total Investment	0.00278	Insignificant Positive Relation
Unemployment	0.00529	Insignificant Positive Relation
Weighted average Call Money Rate	0.004167	Insignificant Positive Relation
Gross Domestic Savings	0.00126	Insignificant Positive Relation
Exports	0.0037	Insignificant Positive Relation
Imports	0.00141	Insignificant Positive Relation
SENSEX	0.00955	Insignificant Positive Relation

Whereas the data analysis shows that equity mutual fund net trading is moderately and negatively related (-48.53%) to net equity FII trading in Indian capital market (Table-2). At the same time, the debt mutual fund net trading is positively but insignificantly related (5.63%) to FII debt trading for the same time period in Indian capital market. Considering net mutual fund investment (X) being the dependent variable and net FII investment (Y) being the independent variable for the data from F.Y. 2010 to F.Y. 2015 the regression equation of mutual fund investment and FII, both equity and debt investments are as follows:-

Regression equation for equity investment	**Regression equation for debt investment**
$X = -0.14\ Y + 722.63$	$X = 1.5\ Y + 30354.05$

IJBARR
E- ISSN -2347-856X
ISSN -2348-0653

Table 2: Showing relationship between FII and Mutual Fund Investments

Year	Karl Pearson's coefficient of correlation (r) with Equity MF Net Purchase/Sales	Degree of Relationship (Significant/Non-significant)	Karl Pearson's coefficient of correlation (r) with Debt MF Net Purchase/Sales	Degree of Relationship (Significant/Non-significant)
2010-2011	-0.83852943	Negative Significant Relationship	0.184470824	Positive Insignificant Relationship
2011-2012	-0.807363611	Negative Significant Relationship	-0.248248363	Negative Insignificant Relationship
2012-2013	-0.726705274	Negative Significant Relationship	-0.128277238	Negative Insignificant Relationship
2013-2014	-0.649031482	Negative Significant Relationship	0.261447536	Positive Insignificant Relationship
2014-2015	-0.593269688	Negative Significant Relationship	-0.33284239	Negative Insignificant Relationship

SUGGESTIONS

Based on the analysis and findings of our research it may be suggested to the investors, both existing and potential, and policy makers regarding Foreign Institutional Investors' behaviour that long term developmental policies for economy should not be based upon inflow of FIIs. Mutual fund should invest more in equity in the stock market and there is much scope to propel the fund channelizing policy making towards Indian debt market. The policy makers may concentrate on this issue.

CONCLUSION

The tourist investment behaviour of the Foreign Institutional Investors that invest their money mainly in financial assets, is very colourful and interesting and is delved by the scholars from different disciplines and countries considering a variety of time periods, economies, events like pre and post economic or financial crisis, data frequencies, etc. The observations of the studies especially that are focusing the Indian situations are contradicting to each other and a bit confusing that leaves the opportunity to the scholars for further studies on the issue.

REFERENCES

1. Bohra, N.S. & Dutt, A. (2011). Foreign Institutional Investment in Indian Capital Market: A Study of Last One Decade. *International Research Journal of Finance and Economics. Issue 68 (2011)*, pp. 103-116. http://www.eurojournals.com/finance.htm; last accessed on 17/09/2012.
2. Bose, Suchismita, 2012, The Impact of FII on Mutual Fund Investment in Stock Market, *IRCA BULLETIN*, Money and Finance, pp- 89-110.
3. Chakrabarti, R. (2001). FII Flows to India: Nature and Causes. *Money and Finance, Vol. 2, No. 7,* October-December 2001. pp. 61-81.
4. Jain, M., Meena, P.L. & Mathur, T.N. (2012). Impact of Foreign Institutional Investment on Stock Market with Special Reference to BSE: A Study of Last One Decade. *Asian Journal of Research in Banking and Finance. Vol.2 Issue 4,* April 2012, pp.31-47.
5. Loomba, J. (2012). Do Fiis Impact Volatility Of Indian Stock Market?. *IRJC International Journal of Marketing, Financial Services & Management Research. Vol. 1, Issue 7,* pp. 80-93. July 2012. www.indianresearchjournals .com; last accessed on 01/04/2013.
6. Ray, Hirak, Lahiri, Abhijit & Sarkar, Joy (2013); Do the Indian Stock Market Traits Influence the Foreign Institutional Investors?, *ANWESHAN, Vol. 1, No 1,* March, 2013, pp. 40-62, Department of Commerce, University of North Bengal.