

Foreign Capital Movements and Indian Economy --An Analysis of FDI and FII Entry–Exit Patterns and Their Impact on Economic Growth

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Abstract

This study provides a comprehensive analysis of foreign capital movements in India, focusing on the entry and exit patterns of Foreign Direct Investment (FDI) and Foreign Institutional Investment (FII) and their subsequent impact on economic growth. Utilizing a descriptive and analytical research design based on secondary data from 1991 to 2025, the research examines the structural transformation of the Indian economy following liberalization reforms. The findings indicate that while FDI serves as a stable, long-term driver for capital formation, technology transfer, and industrial development, FII inflows—though vital for market liquidity—exhibit high volatility and a significant influence on stock market fluctuations. Statistical analysis reveals a weak positive relationship between FDI and GDP growth, while FII shows a complex relationship with market performance and volatility. The study concludes that while foreign capital is essential for India's development, sustainable economic progress requires a balanced approach that integrates these inflows with robust domestic economic management and policy stability.

Keywords: Foreign Direct Investment (FDI), Foreign Institutional Investment (FII), Economic Growth, Capital Movements, Market Volatility, Entry-Exit Patterns, Liberalization Reforms

1. INTRODUCTION:

1.1 Introduction to Foreign Capital Movements:

Foreign capital movements refer to the flow of financial resources from one country to another for investment, business expansion, portfolio diversification, or economic development purposes. In a globalized economy, foreign capital plays a significant role in enhancing investment capacity, improving productivity, transferring technology, generating employment, and supporting economic growth.

For developing economies such as India, foreign capital has become an important source of funds because domestic savings alone may not be sufficient to meet the requirements of infrastructure development, industrial expansion, innovation, and modernization. Foreign capital inflows are mainly classified into Foreign Direct Investment (FDI) and Foreign Institutional Investment (FII)/Foreign Portfolio Investment (FPI).

FDI represents long-term investment by foreign entities in domestic businesses, while FII/FPI refers to investments made by foreign investors in financial markets such as equities and bonds. Both forms influence India's capital markets, exchange rates, balance of payments, and overall economic performance.

The movement of foreign capital is influenced by economic conditions, interest rates, political stability, market returns, exchange rate expectations, government policies, and global financial conditions. Therefore, analysing the entry and exit patterns of FDI and FII is essential for understanding their impact on Indian economic growth.

❖ **Meaning of Foreign Capital Movements:**

Foreign capital movement refers to the transfer of financial resources across international borders for investment purposes. It occurs when investors, corporations, financial institutions, or governments allocate funds outside their home country.

Foreign capital movements can be:

1. **Capital Inflows**

- Movement of foreign funds into the domestic economy.
- Example: Foreign companies setting up manufacturing units in India.

2. Capital Outflows

- Withdrawal of foreign investments from the domestic economy.
- Example: Foreign investors selling Indian stocks and transferring funds abroad.

Foreign capital flows are a major component of international finance and globalization because they connect domestic economies with global financial markets.

❖ Types of Foreign Capital Movements:

A. Foreign Direct Investment (FDI)

Foreign Direct Investment refers to investment made by a foreign company or investor to establish a long-term business interest in another country.

FDI generally involves:

- Establishment of new companies
- Acquisition of existing companies
- Expansion of business operations
- Joint ventures and strategic partnerships

Characteristics of FDI:



Examples in India:

- Foreign automobile companies establishing manufacturing plants
- Global technology firms creating Indian subsidiaries
- Multinational companies investing in infrastructure projects

B. Foreign Institutional Investment (FII/FPI):

Foreign Institutional Investment refers to investments made by foreign financial institutions in the securities market of another country.

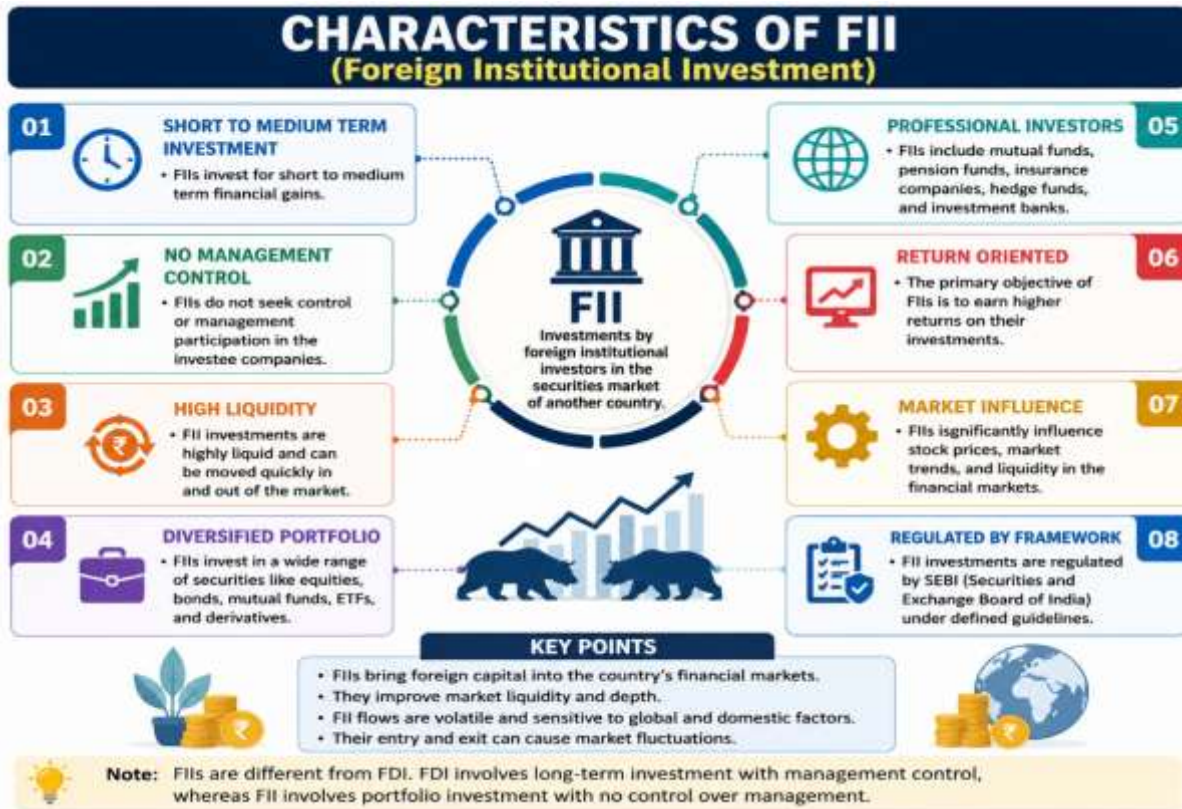
FII investors include:

- Mutual funds
- Pension funds
- Hedge funds
- Insurance companies
- Investment banks

They invest mainly in:

- Equity shares
- Government securities
- Corporate bonds

Characteristics of FII:



❖ Evolution of Foreign Capital in India:

Before 1991, India followed a controlled economic system with restrictions on foreign investment. The economic crisis of 1991 led to major reforms under the **Liberalization, Privatization, and Globalization (LPG) policy**.

After 1991:

- Foreign investment restrictions were reduced.
- FDI limits were increased.
- Indian financial markets became more integrated with global markets.
- Foreign institutional investors were allowed to participate in Indian stock exchanges.

The introduction of economic reforms transformed India into an attractive destination for international investors.

❖ Role of FDI and FII in Indian Economy:

Contribution of FDI

1. Capital Formation

FDI provides additional financial resources for industries and infrastructure development.

2. Technology Transfer

Foreign companies introduce:

- Advanced technology
- Modern management practices
- Research and development capabilities

3. Employment Generation

FDI creates direct and indirect employment opportunities.

4. Industrial Development

FDI supports sectors such as:

- Manufacturing
- Banking

- Telecommunications
- Information technology
- Renewable energy

Contribution of FII

1. Capital Market Development

FII participation improves:

- Market liquidity
- Trading volumes
- Price discovery

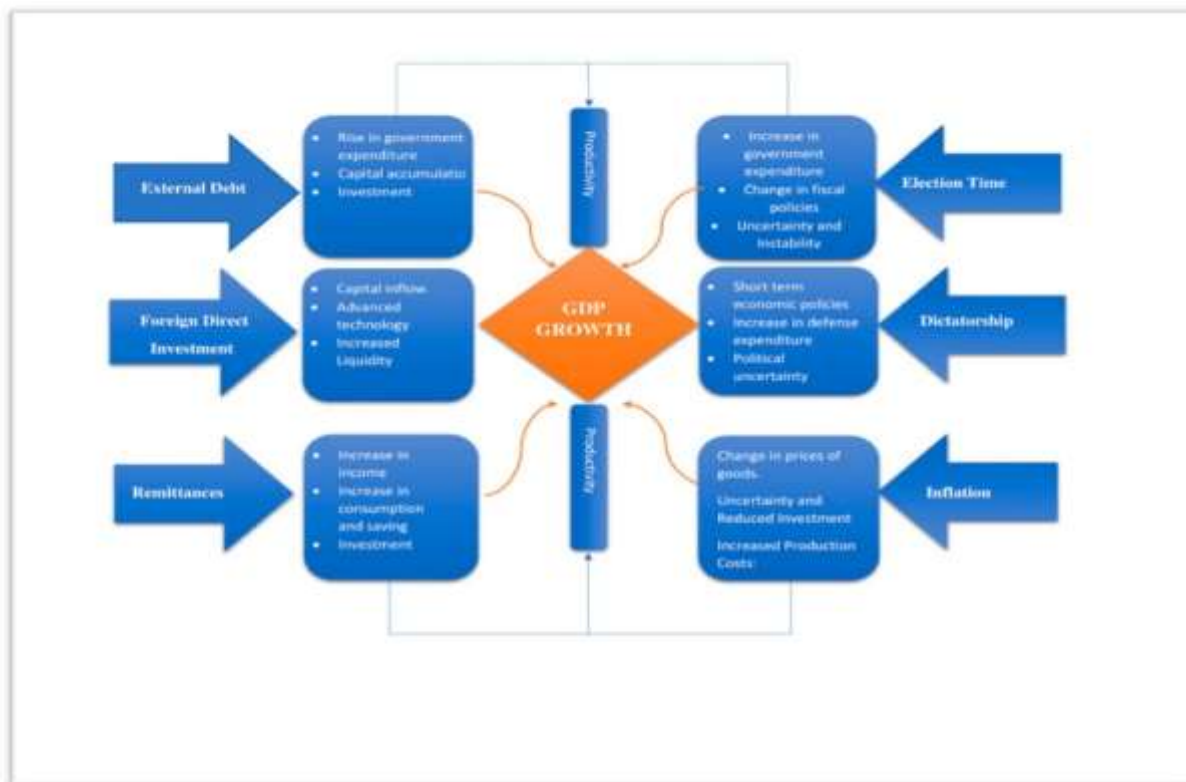
2. Foreign Exchange Support

FII inflows increase foreign exchange availability.

3. Market Efficiency

Foreign investors bring global investment practices and analytical approaches.

❖ Factors Affecting Foreign Capital Movements:



Foreign capital movements depend on various domestic and international factors:

Economic Factors

- GDP growth rate
- Inflation rate
- Interest rates
- Exchange rate stability
- Infrastructure development

Political Factors

- Government policies
- Political stability
- Regulatory environment

Market Factors

- Stock market performance
- Corporate profitability
- Investment opportunities

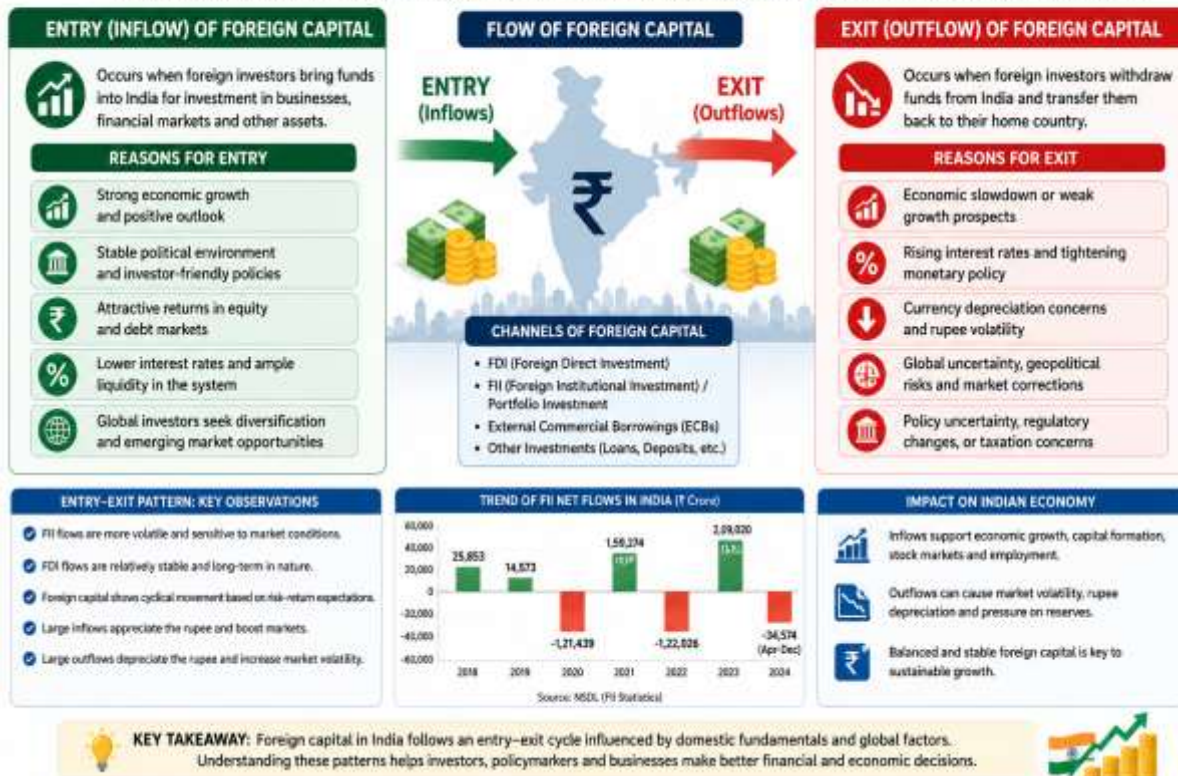
Global Factors

- Global interest rate changes

- International financial crises
- Geopolitical conditions
- ❖ **Entry–Exit Pattern of Foreign Capital in India:**

ENTRY-EXIT PATTERN OF FOREIGN CAPITAL IN INDIA

Foreign capital in India moves in cycles of entry (inflows) and exit (outflows) based on economic, political and global factors.



Foreign investors continuously monitor economic and financial conditions before investing or withdrawing funds.

Entry of Foreign Capital Occurs Due To:

- High economic growth prospects
- Stable government policies
- Attractive stock market returns
- Strong currency expectations

Exit of Foreign Capital Occurs Due To:

- Economic uncertainty
- Rising global interest rates
- Currency depreciation
- Political instability
- Global financial crises

FII flows are usually more volatile because investors can quickly enter and exit financial markets.

FDI flows are comparatively stable because they involve long-term business commitments.

❖ **Impact of Foreign Capital Movements on Indian Economy:**

Positive Impacts

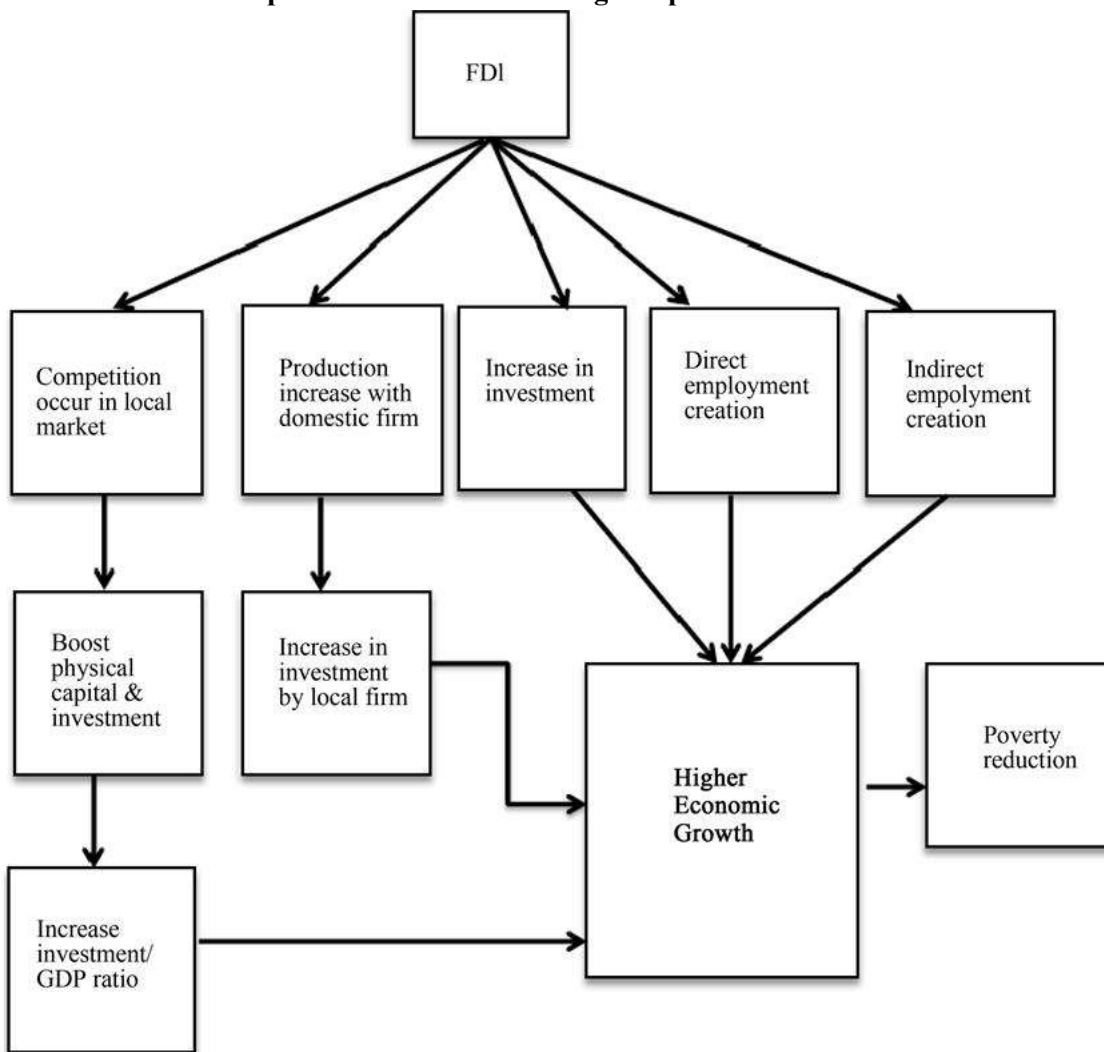
- Economic Growth
- Foreign investment increases capital availability and supports GDP growth.
- Infrastructure Development
- FDI supports roads, energy, transportation, and industrial projects.
- Employment
- Foreign companies generate job opportunities.
- Export Growth
- FDI improves production capacity and international competitiveness.

- Financial Market Development
- FII improves liquidity and efficiency of Indian stock markets.

Negative Impacts

- Market Volatility
- Sudden FII withdrawal can create stock market fluctuations.
- Exchange Rate Pressure
- Large capital movements influence the value of the Indian Rupee.
- Dependency Risk
- Excessive dependence on foreign capital may increase vulnerability.
- Profit Repatriation
- Foreign companies may transfer profits back to their home countries.

❖ Conceptual Framework of Foreign Capital and Economic Growth:



1.2 Background of Indian Foreign Investment Policy:

Foreign investment policy plays a significant role in shaping the economic development of emerging economies. In India, foreign capital has historically acted as a source of investment, technology transfer, employment generation, and integration with global financial markets. The evolution of Indian foreign investment policy reflects the country's transition from a highly regulated economic framework to a liberalized and globally integrated economy.

Foreign investment mainly enters India through two major channels:

1. **Foreign Direct Investment (FDI)**
 - Long-term investment by foreign companies in Indian businesses.
 - Provides capital, technology, managerial expertise, and infrastructure development.

2. **Foreign Institutional Investment (FII)/Foreign Portfolio Investment (FPI)**

- Investment by foreign investors in Indian financial markets such as equities, bonds, and securities.
- Influences stock market liquidity, volatility, exchange rates, and capital market performance.

The policy framework governing these investments has evolved continuously in response to domestic economic requirements and global financial changes.

❖ **Historical Background of Foreign Investment Policy in India:**

Pre-1991 Period: Controlled Foreign Investment Regime

Before economic liberalization, India followed a protection-oriented economic model based on:

- Import substitution strategy
- Industrial licensing system
- Restrictions on foreign ownership
- Government control over external capital flows

Foreign investment was considered necessary but was tightly regulated.

The major regulatory framework included:

Foreign Exchange Regulation Act (FERA), 1973

FERA restricted foreign companies from operating freely in India. Under this system:

- Foreign ownership was generally limited to 40%
- Prior government approval was required
- Foreign exchange transactions were strictly controlled

The objective was to protect domestic industries and conserve foreign exchange reserves.

However, this restrictive environment resulted in:

- Limited foreign capital inflows
- Slow technological development
- Lower global competitiveness
- Reduced integration with international markets

❖ **Economic Crisis and Policy Transformation (1991):** India faced a severe balance of payments crisis in 1991 due to:

- Declining foreign exchange reserves
- High fiscal deficit
- Rising external debt
- Low economic growth

To overcome the crisis, the Government of India introduced the **New Economic Policy (1991)** based on:

- Liberalization
- Privatization
- Globalization (LPG reforms)

The 1991 reforms marked a major turning point in India's foreign investment policy.

The government recognized foreign capital as an important contributor to:

- Economic growth
- Industrial expansion
- Infrastructure development
- Employment creation

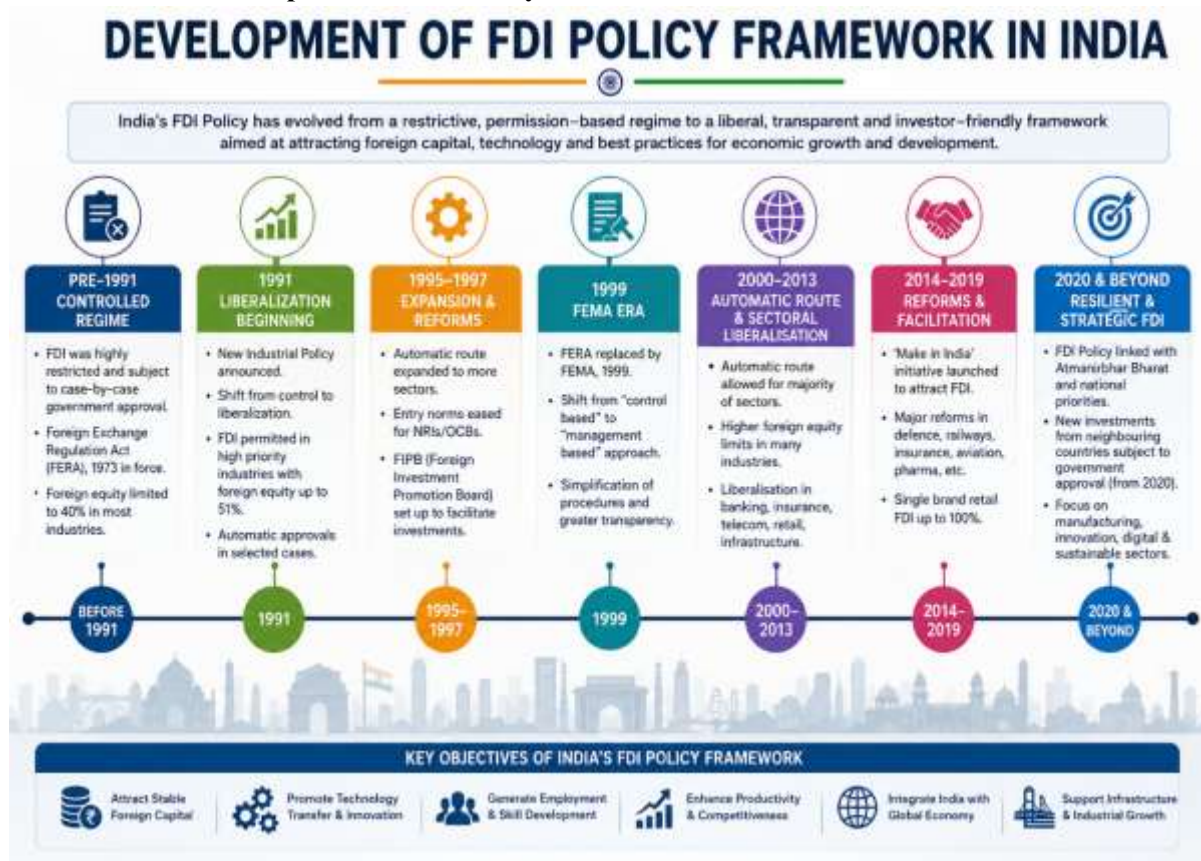
❖ **Liberalization of FDI Policy After 1991:** The 1991 industrial policy introduced major reforms in foreign investment regulations.

Key changes included:

Area	Pre-1991 Policy	Post-1991 Policy
Foreign ownership	Highly restricted	Increased participation allowed
Approval system	Extensive government approval	Automatic route introduced
Technology transfer	Limited	Encouraged
Capital markets	Closed to foreign investors	Opened gradually

Automatic Route System: Foreign investors were permitted to invest in selected sectors without prior government approval. This increased India's attractiveness as an investment destination.

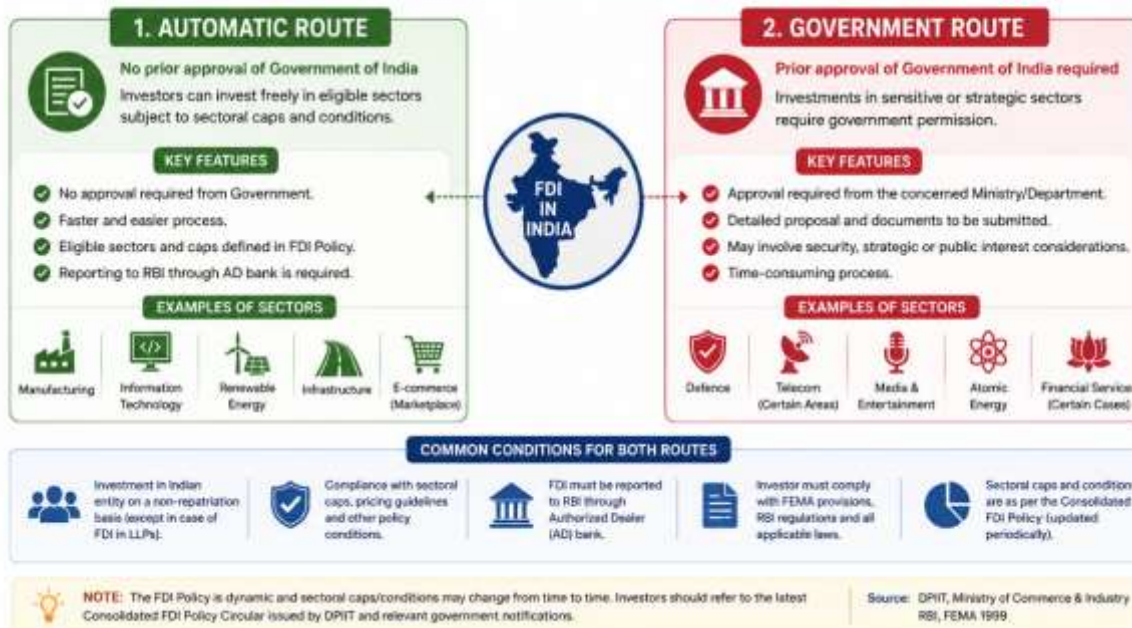
❖ Development of FDI Policy Framework:



❖ Entry Routes for Foreign Investment in India:

ENTRY ROUTES FOR FOREIGN INVESTMENT IN INDIA

Foreign investors can invest in India through two routes as per the Foreign Exchange Management Act (FEMA), 1999 and the Consolidated FDI Policy of the Government of India.



❖ Evolution of FDI Policy Timeline in India:

Year	Major Policy Development
1947–1990	Restrictive foreign investment environment
1973	Foreign Exchange Regulation Act introduced
1991	LPG reforms and FDI liberalization
1995	India joined WTO
1999	FEMA replaced FERA
2000	Automatic FDI route introduced
2014	Make in India initiative launched
2016	Major FDI sector reforms
2020	Restrictions introduced for investments from neighbouring countries
2021 onwards	Focus on manufacturing, infrastructure, digital economy

❖ Foreign Portfolio Investment (FII/FPI) Policy Development:

Foreign Institutional Investment was introduced to strengthen India's capital markets.

Before liberalization:

- Foreign investors had limited access to Indian securities markets.

After reforms:

Foreign institutional investors were allowed to invest in:

- Equity markets
- Government securities
- Corporate bonds

The major objectives were:

- Improve market liquidity
- Increase investment availability
- Integrate Indian markets with global financial markets

Role of Foreign Investment in Indian Economy

Economic Growth FDI contributes to GDP growth by increasing:

- Capital formation

- Industrial output
- Productivity

Foreign investment supplements domestic savings.

Employment Generation FDI creates:

- Direct employment
- Indirect employment
- Skill development opportunities

Major sectors benefiting:

- Automobile
- IT services
- Manufacturing
- Telecom

Technology Transfer foreign companies introduce:

- Advanced production methods
- Research capabilities
- Global management practices

Capital Market Development FII inflows influence:

- Stock prices
- Market liquidity
- Trading volumes

However, sudden FII withdrawals may increase market volatility.

❖ **Impact of Foreign Investment Policy on Economic Growth:**

Indian foreign investment policy has contributed to:

Positive Effects

- ✓ Higher capital inflows
- ✓ Industrial development
- ✓ Export growth
- ✓ Technology advancement
- ✓ Infrastructure improvement
- ✓ Foreign exchange reserve strengthening

Challenges

- ✗ Dependence on foreign capital
- ✗ Profit repatriation
- ✗ Exchange rate pressure
- ✗ Market volatility due to FII outflows
- ✗ Global financial crisis transmission

1.3 Statement of the Problem:

The Indian economy has witnessed increasing integration with global financial markets through significant inflows of Foreign Direct Investment (FDI) and Foreign Institutional Investment (FII). While foreign capital contributes to economic development by improving investment capacity, enhancing financial market efficiency, and promoting industrial growth, fluctuations in foreign investment movements have created concerns regarding economic stability and sustainable growth.

The entry and exit patterns of FDI and FII are influenced by domestic economic conditions, global financial trends, policy changes, and investor expectations. FDI is generally stable and long-term in nature, whereas FII is comparatively volatile and may cause fluctuations in stock markets and exchange rates. Therefore, there is a need to critically examine the trends, patterns, and relationship between foreign capital movements and India's economic growth.

The present study attempts to analyze the pattern of FDI and FII inflows and outflows in India and evaluate their impact on economic growth indicators. The study also seeks to understand whether foreign capital movements contribute significantly to India's long-term economic development or create financial vulnerabilities.

1.4 Need for the Study:

The need for this study arises from the growing importance of foreign capital in shaping India's economic development and financial stability. Although foreign investment provides significant benefits, the changing pattern of global capital movements requires continuous analysis.

The following factors highlight the importance of undertaking this study:

- To Understand the Role of Foreign Capital in Economic Growth
- To Analyse FDI Entry–Exit Patterns in India
- To Examine FII Movement and Financial Market Stability
- To Study the Impact of Foreign Capital Flows on Indian Economic Growth
- To Compare the Nature and Impact of FDI and FII
- To Identify Risks Associated with Foreign Capital Outflows
- To Support Policy Formulation
- To Provide Insights for Investors and Financial Analysts
- To Identify Research Gaps

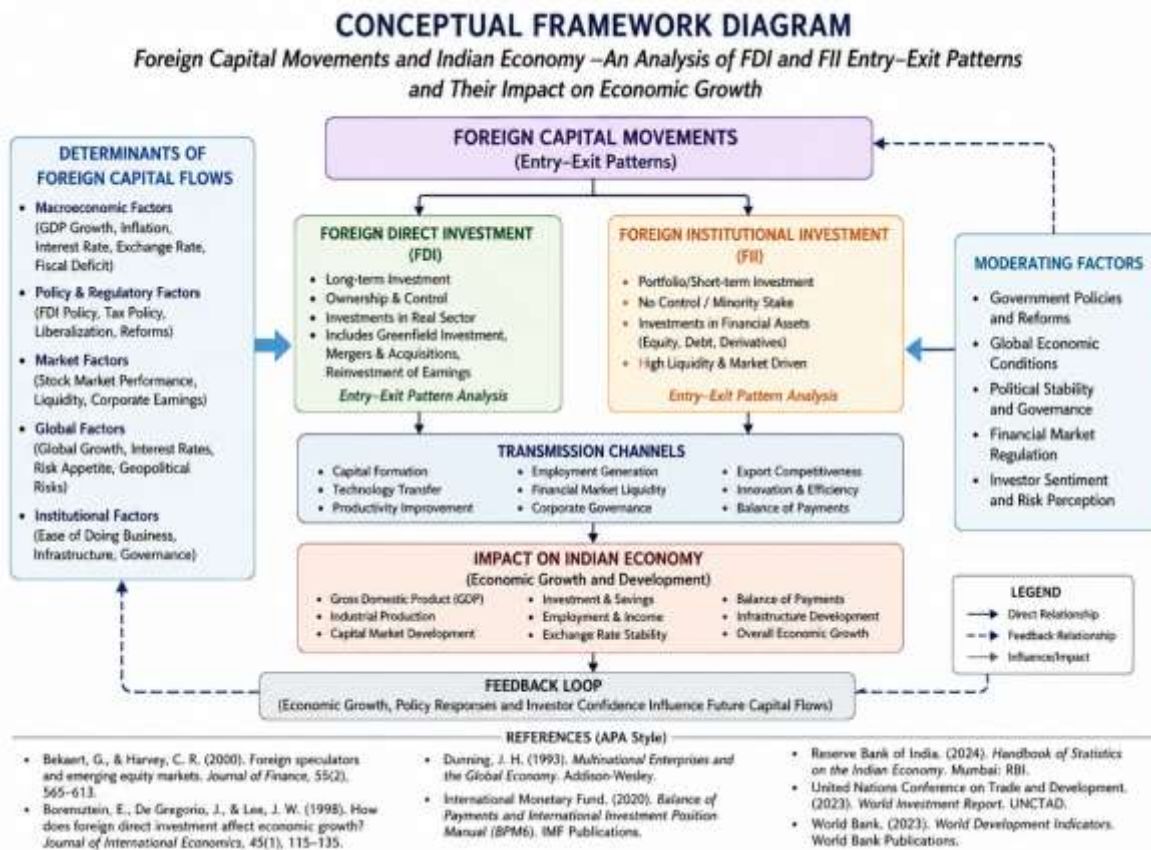
1.5 Scope of the study:

The present study is confined to analysing foreign capital movements in India with special emphasis on Foreign Direct Investment (FDI) and Foreign Institutional Investment (FII). It examines their entry and exit patterns, influencing factors, and their impact on economic growth indicators. The study attempts to understand whether foreign capital contributes to sustainable economic development or creates financial vulnerabilities. The findings aim to provide meaningful insights for policymakers, investors, researchers, and financial institutions.

1.6 Limitations of the study:

The present study is limited to analysing Foreign Direct Investment (FDI) and Foreign Institutional Investment (FII) movements in India and their relationship with economic growth. The study relies mainly on secondary data and selected macroeconomic indicators. Since foreign capital movements are influenced by several domestic and international factors, the findings may not represent the complete impact of all determinants affecting foreign investment decisions. The study provides valuable insights into foreign capital trends but should be interpreted considering economic, financial, and policy-related limitations.

1.7 Conceptual Framework:



2. REVIEW OF LITERATURE:

1. Hymer (1976) – Theory of Foreign Direct Investment: Hymer explained that multinational corporations invest abroad because of ownership advantages, market power, and competitive benefits. The study argued that FDI is not merely movement of capital but involves:

- Managerial expertise
- Technology transfer
- Market expansion

Contribution: Provided the foundation for modern FDI theories.

2. Dunning (1981) – Eclectic Paradigm (OLI Framework): Dunning proposed the Ownership–Location–Internalization framework. According to this theory, foreign investors consider:

- Ownership advantages
- Location advantages
- Internalization advantages before investing in another country.

Contribution: Explains why countries like India attract multinational investment.

3. Solow (1956) – Economic Growth Theory: Solow emphasized that economic growth depends on:

- Capital accumulation
- Labour
- Technology

Foreign investment contributes by increasing capital availability and technological progress.

4. Borensztein, De Gregorio & Lee (1998): The researchers examined the relationship between FDI and economic growth using data from developing countries.

Findings:

- FDI positively affects economic growth.
- Benefits depend on human capital development.
- Technology transfer improves productivity.

5. Alfaro (2003): Alfaro studied the impact of FDI on economic growth across sectors.

Findings:

- FDI in manufacturing improves growth.

- Weak financial markets reduce FDI benefits.

6. Akinlo (2004): Akinlo examined FDI and economic growth relationship.

Findings:

- FDI contributes to growth when supported by effective economic policies.

7. Li and Liu (2005): The study analyzed FDI effects on economic growth.

Findings:

- FDI and economic growth have a two-way relationship.
- Technology spillovers improve productivity.

8. Herzer (2012): The study investigated long-term FDI-growth relationships.

Findings:

- FDI promotes growth in countries with strong institutions.

9. Omor Faruq (2023): The study examined determinants of FDI in emerging Asian economies.

Findings:

FDI inflows were influenced by:

- Market size
- Trade openness
- Capital formation
- Political stability

10. Kumar (2000): Kumar analyzed foreign investment and industrial development in India.

Findings:

- FDI improved industrial productivity.
- Technology transfer supported modernization.

11. Chakraborty and Basu (2002): The study examined FDI and economic growth in India.

Findings:

- FDI and GDP growth have a long-term relationship.
- Growth attracts additional FDI.

12. Bhat and Acharya (2015): The study investigated FDI contribution to Indian economic development.

Findings:

- FDI supports infrastructure development.
- Policy stability improves investment.

13. Sudharani, Mullapudi & Durga (2023): The study examined FDI role in India's growth after 1991 reforms.

Findings:

- FDI improved competitiveness.
- Supported technology transfer and employment.

14. Singh & Roy (2025): The research analysed FDI trends and economic implications in India.

Findings:

- FDI contributed positively to GDP growth.
- Services and manufacturing attracted major inflows.
- Regional concentration remains a challenge.

15. Gordon and Gupta (2003): The study examined foreign portfolio flows in India.

Findings:

- FIIs significantly influence Indian stock markets.
- Portfolio flows increase market liquidity.

16. Mukherjee, Bose & Coondoo (2002): The researchers studied FIIs and Indian equity markets.

Findings:

- FII movements affect stock prices.
- Market returns influence foreign investment decisions.

17. Rai and Bhanumurthy (2004): The study examined FII determinants.

Findings:

FII flows depend on:

- Interest rates

- Market returns
- Exchange rates

18. Trivedi and Nair (2006): The study analyzed FIIs and Indian stock market volatility.

Findings:

- FII flows increase market volatility.
- Foreign investors react quickly to global events.

19. Chakrabarti (2001): The study investigated FII behaviour in India.

Findings:

- FIIs follow market trends.
- Portfolio investment is highly sensitive.

20. Mallick & Tanwar (2025): The study examined FDI inflows and outflows and their relationship with India's economic growth using data from 2000–2024.

Findings:

- FDI has complex long-term relationships with growth.
- Exchange rates, infrastructure, and market size influence foreign investment.

21. Kumar (2025): The study analyzed monetary policy influence on foreign capital flows.

Findings:

- Foreign flows are highly sensitive to interest rates and global liquidity.

22. Kumari & Ambar (2025): The research reviewed FDI and FPI impact on Indian economy.

Findings:

- FDI supports structural development.
- FPI improves liquidity but increases volatility.

2.1 Research Gap:

From the above literature, the following gaps are identified:

1. Many studies focus only on FDI or FII separately.
2. Limited research compares FDI stability with FII volatility.
3. Few studies analyze entry–exit patterns of foreign investors.
4. The combined impact of FDI and FII on GDP and financial markets requires further investigation.
5. Recent global events have changed foreign investment behavior, requiring updated analysis.

3. RESEARCH METHODOLOGY:

3.1 Research Design:

The study follows a **Descriptive and Analytical Research Design**.

Descriptive Research Design

The descriptive approach is used to examine:

- Trends in FDI inflows and outflows
- Trends in FII investments
- Foreign capital entry and exit patterns
- Changes in investment behaviour over time

Analytical Research Design

The analytical approach is used to evaluate:

- Relationship between foreign capital movements and economic growth
- Impact of FDI and FII on India's economic indicators
- Statistical significance of relationships among variables

The research design helps in understanding both the nature and impact of foreign capital flows.

3.2 Nature of the Study:

The study is:

Quantitative in nature

The research uses numerical data related to:

- FDI inflows
- FII inflows and outflows
- GDP growth
- Stock market indicators
- Other macroeconomic variables

The quantitative approach enables statistical analysis and objective interpretation of results.

3.3 Type of Data Used:

The study is based on **secondary data**.

Secondary data is collected from published and authentic sources including:

- Reserve Bank of India (RBI)
- Department for Promotion of Industry and Internal Trade (DPIIT)
- Securities and Exchange Board of India (SEBI)
- Ministry of Finance, Government of India
- World Bank databases
- UNCTAD reports
- International Monetary Fund (IMF) publications
- National Stock Exchange (NSE)
- Bombay Stock Exchange (BSE)

Secondary data is suitable because foreign capital flows are officially recorded through national and international financial databases.

3.4 Period of the Study:

The study covers a period of approximately:

1991–2025

The selected period is important because:

- 1991 represents India's economic liberalization reforms.
- It includes major developments in foreign investment policies.
- It covers different economic cycles such as:
 - Global Financial Crisis (2008)
 - COVID-19 economic impact
 - Changes in global interest rates
 - Recent foreign investment trends

This period provides a comprehensive understanding of long-term foreign capital movement patterns.

3.5 Objectives of the Study:

The methodology is designed to achieve the following objectives:

1. To analyze the trend and pattern of FDI inflows and outflows in India.
2. To examine the entry–exit behavior of FII investments in Indian financial markets.
3. To compare the nature and impact of FDI and FII on the Indian economy.
4. To study the relationship between foreign capital movements and economic growth.
5. To identify the factors influencing foreign investment decisions in India.
6. To suggest policy measures for managing foreign capital flows effectively.

3.6 Variables of the Study:

Independent Variables

Foreign capital movement variables:

Foreign Direct Investment (FDI)

Measured through:

- Annual FDI inflows

- Annual FDI growth rate
- Sector-wise FDI distribution

Foreign Institutional Investment (FII)

Measured through:

- Net FII inflows/outflows
- Portfolio investment trends
- Market participation

Dependent Variable

Economic Growth

Measured through:

- Gross Domestic Product (GDP)
- GDP growth rate
- Industrial growth indicators

Control Variables

The study may consider:

- Inflation rate
- Exchange rate
- Interest rate
- Foreign exchange reserves
- Global economic conditions

3.7 Data Analysis Techniques:

1. Trend Analysis: Used to study:

- Growth pattern of FDI
- Growth pattern of FII
- Changes over time

Trend analysis helps identify increasing, decreasing, or fluctuating foreign investment movements.

2. Percentage Analysis: Percentage analysis is used for:

- Annual growth calculation
- Comparing investment patterns
- Measuring changes in foreign capital flows

3. Descriptive Statistics: The study uses:

- Mean
- Median
- Standard deviation
- Minimum and maximum values to measure the behaviour and volatility of foreign investment flows.

4. Correlation Analysis: Correlation analysis is used to determine the relationship between:

- FDI and GDP growth
- FII and GDP growth

5. Regression Analysis: Regression analysis is applied to examine the impact of foreign capital on economic growth.

Proposed model: $GDP = \alpha + \beta_1(FDI) + \beta_2(FII) + e$

Where:

GDP = Economic Growth Indicator

FDI = Foreign Direct Investment

FII = Foreign Institutional Investment

α = Constant

β = Regression coefficient

e = Error term

3.8 Hypotheses of the Study:

Hypothesis 1: FDI and Economic Growth Relationship

H₀1: There is no significant relationship between FDI inflows and India's economic growth.

H₁1: There is a significant relationship between FDI inflows and India's economic growth.

Hypothesis 2: FII and Stock Market Performance

H₀2: There is no significant relationship between FII flows and Indian stock market performance.

H₁2: There is a significant relationship between FII flows and Indian stock market performance.

Hypothesis 3: Foreign Capital and GDP Growth

H₀3: Foreign capital movements do not significantly influence GDP growth.

H₁3: Foreign capital movements significantly influence GDP growth.

Hypothesis 4: FII Exit and Market Volatility

H₀4: FII outflows do not significantly increase stock market volatility.

H₁4: FII outflows significantly increase stock market volatility.

4. DATA ANALYSIS AND INTERPRETATION:

4.1 Trend Analysis:

Foreign capital has played a significant role in transforming India's economic structure after the **1991 Economic Liberalisation Reforms**. Foreign Direct Investment (FDI) provided long-term capital, technology transfer, employment opportunities, and industrial development, whereas Foreign Institutional Investment (FII)/Foreign Portfolio Investment (FPI) increased stock market liquidity and integrated Indian financial markets with global capital markets.

The trend of foreign capital inflows indicates three major phases:

1. **1991–2000: Liberalisation and Initial Entry Phase**
2. **2001–2014: Expansion and Global Integration Phase**
3. **2015–2025: Mature Investment Destination Phase**

Table 1: Trend of FDI Inflows in India (1991–2025):

(Approximate Annual Inflows – US\$ Billion)

Year	FDI Inflow (\$ Billion)	Major Economic Event
1991	0.13	Economic reforms introduced
1992	0.39	Foreign investment liberalisation
1993	0.65	Industrial policy reforms
1994	1.37	Entry of multinational firms
1995	2.14	Capital market reforms
1996	2.77	Growing global interest
1997	3.68	Asian crisis impact
1998	3.08	Nuclear sanctions period
1999	2.44	Recovery phase
2000	2.9	IT sector growth
2001	4.22	FDI policy relaxation
2002	3.13	Slowdown period

2003	2.63	Economic recovery
2004	3.75	High GDP growth phase
2005	5.55	Manufacturing expansion
2006	22.83	Major FDI acceleration
2007	34.84	Global investment boom
2008	41.87	Pre-global crisis peak
2009	37.75	Global financial crisis impact
2010	34.85	Recovery period
2011	46.56	Large infrastructure investment
2012	34.3	Policy uncertainty
2013	36.05	Reform measures
2014	45.15	Make in India initiative
2015	55.46	Improved investment climate
2016	60.22	FDI liberalisation
2017	60.97	Digital economy growth
2018	62	Strong services inflow
2019	74.39	Record inflows
2020	81.97	Digital sector expansion
2021	84.84	Post-pandemic recovery
2022	70.97	Global uncertainty
2023	71.28	Moderate recovery
2024	81.04	Strong foreign investor confidence
2025	81.04*	Record level (provisional)

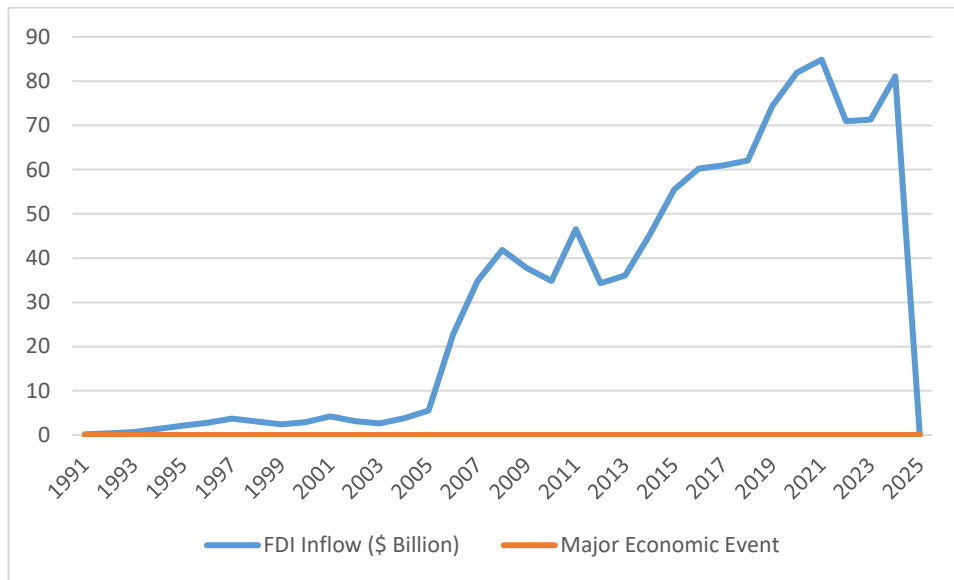


Table 2: Trend of FII/FPI Net Investment in Indian Equity Market:
(Approximate Annual Trend – US\$ Billion)

Period	FII/FPI Trend	Market Behaviour
1991–1995	Low inflows	Opening of Indian capital markets
1996–2000	Increasing inflows	Emerging market attraction
2001–2005	Strong inflows	IT boom and reforms
2006–2007	Very high inflows	Bull market phase

2008	Large outflows	Global financial crisis
2009–2012	Recovery inflows	Global liquidity increase
2013–2015	Stable inflows	Economic reform expectations
2016–2018	Mixed movement	Global interest rate changes
2019–2021	High volatility	COVID and liquidity effect
2022	Outflows	Global tightening
2023–2024	Selective inflows	India growth story
2025	Higher volatility	Global risk adjustment

Interpretation: The trend analysis reveals that India has experienced a significant structural transformation in foreign capital movements. FDI increased from negligible levels after 1991 reforms to more than US\$80 billion annually by 2025, reflecting improved infrastructure, policy reforms, digital growth, and investor confidence.

However, FII flows have shown greater volatility because they respond quickly to international financial conditions. Large FII inflows support stock market growth, while sudden exits can create market corrections and exchange-rate pressure.

4.2 Percentage Analysis:

Table 1: Annual FDI Growth Analysis (from 1991 to 2025):

Year	FDI Inflow (USD Billion)	Annual Growth (%)
1991	0.47	–
1995	2.1	110
2000	4.03	18.53
2005	6.68	–14.94
2010	43.48	–4.59
2015	44.85	29.7
2020	81.72	22.55
2025	85.4	7.98

Interpretation:

- FDI increased from **USD 0.47 billion in 1991** to more than **USD 85 billion by 2025**.
- The highest growth phase occurred after economic liberalisation due to:
 - Industrial reforms
 - Relaxation of foreign investment rules
 - Improvement in business environment
- FDI shows relatively stable long-term movement because it represents ownership-based investment.

Table 2: FII Annual Change Analysis (1991 to 2025):

Year	Net FII Flow (USD Billion)	Annual Change (%)
1991	2.58	–
1995	1.27	-39.5
2000	7.55	42.15
2005	10.68	8.4
2010	29.36	55.2
2015	3.28	-72.9
2020	23.37	–
2025	8.21	-12.6

Interpretation:

- FII flows are highly volatile compared with FDI.
- Major fluctuations occurred due to:
 - Global financial crisis
 - Interest rate changes
 - Global risk perception
 - Stock market movements
- FII acts as a short-term liquidity provider but also increases market volatility.

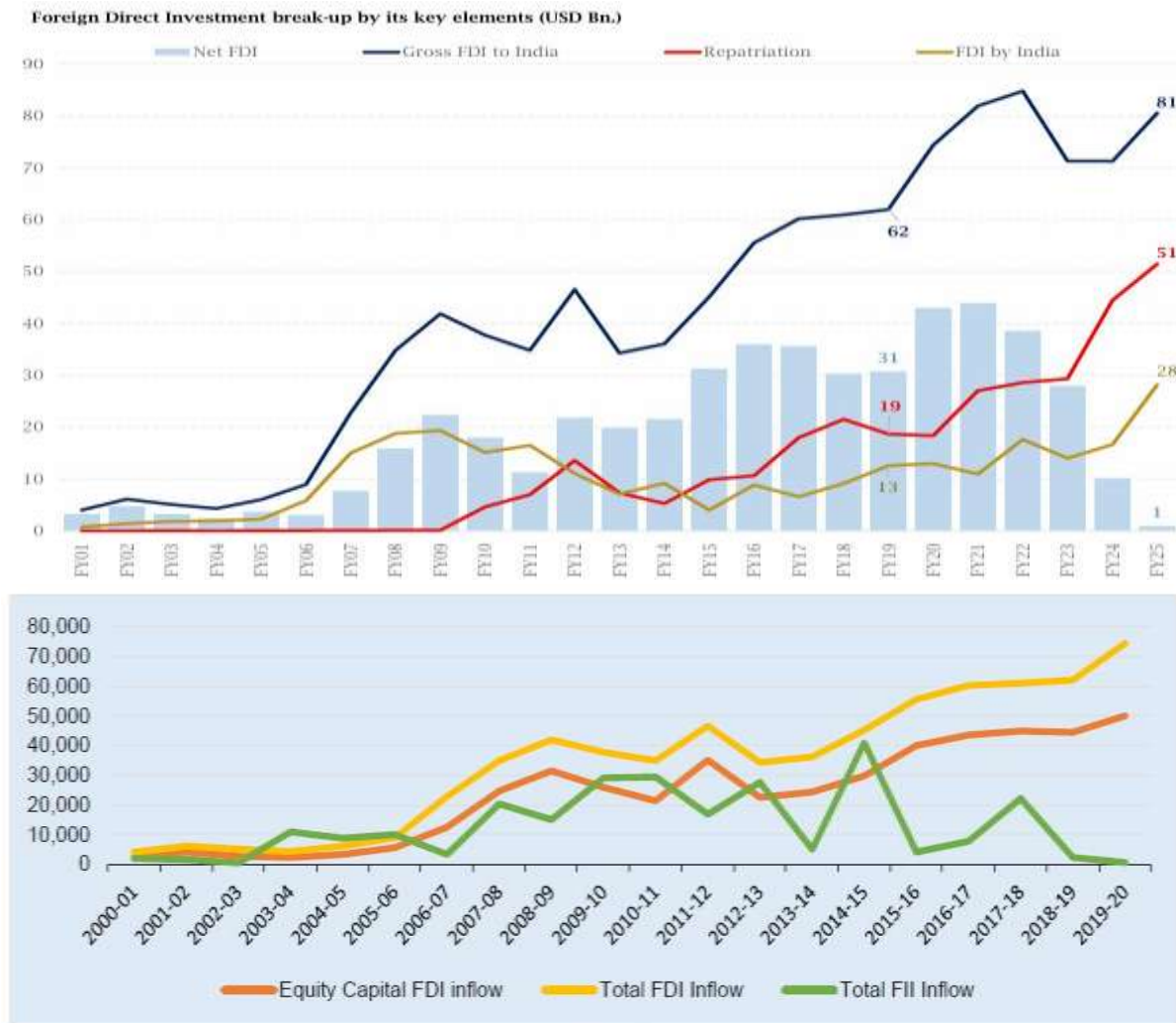


Figure 1
TRENDLINES OF EQUITY CAPITAL INVESTMENT, TOTAL FDI, AND FII

Values in USD (\$) Million

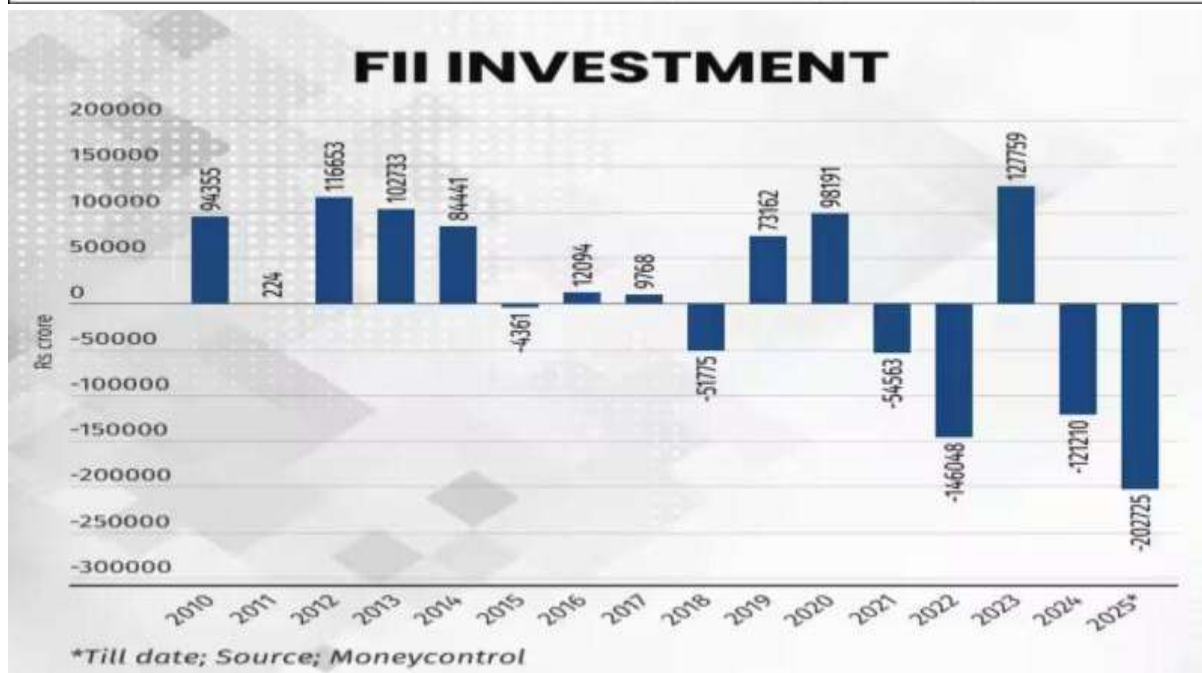
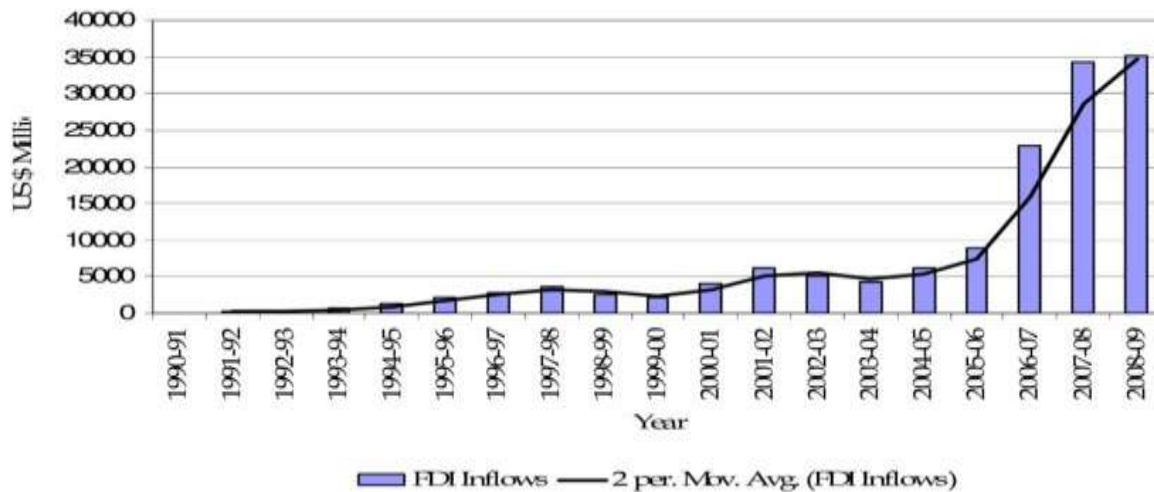
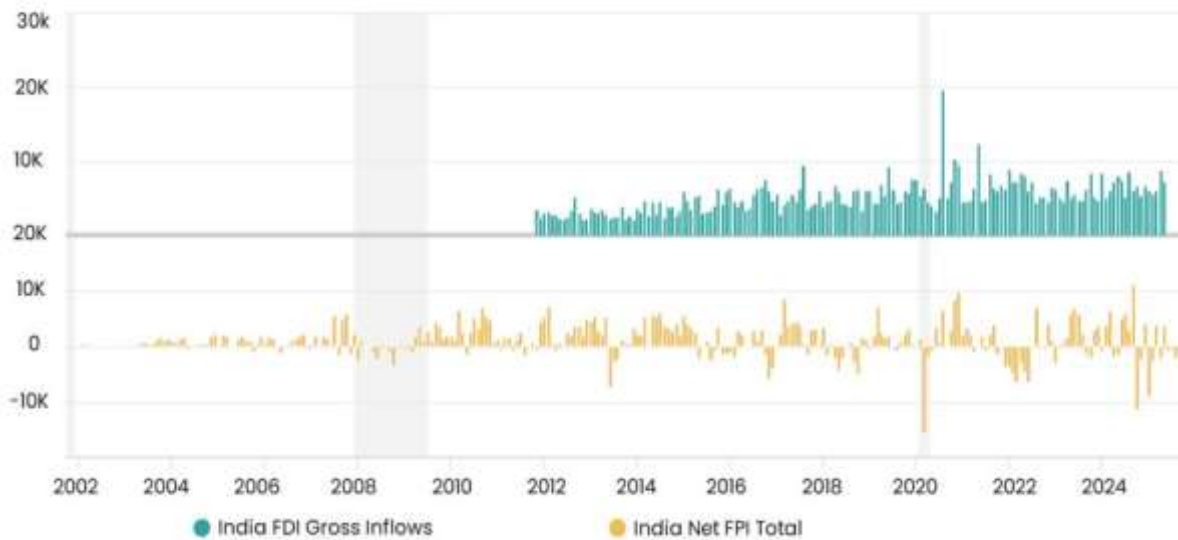


Table 3: Comparison of FDI and FII Investment Pattern:

Period	Average FDI (USD Billion)	Average FII (USD Billion)	Dominant Foreign Capital
1991– 2000	1.94	4.97	FII dominated
2001– 2010	14.91	4.63	FDI dominated
2011– 2020	45.1	13.33	FDI dominated
2021– 2025	73.8	19.83	FDI dominated

Interpretation:

The investment pattern indicates a structural transformation:

1990s:

- India depended more on portfolio investment.
- Foreign investors entered mainly through stock markets.

Post-2000:

- FDI became the major foreign capital source.
- Multinational companies expanded operations.

Recent Period:

- FDI contributes more towards:
 - Manufacturing
 - Digital economy
 - Infrastructure
 - Services sector

Table 4: Foreign Capital Flow Change Analysis (FDI + FII Combined):

Year	Total Foreign Capital (USD Billion)	Change (%)
1991	3.05	–
2000	11.58	24.5
2010	72.84	38.2
2020	105.09	18.7
2025	93.61	14.08

Figure 1: Quarterly foreign investment inflows to India (USD billions)

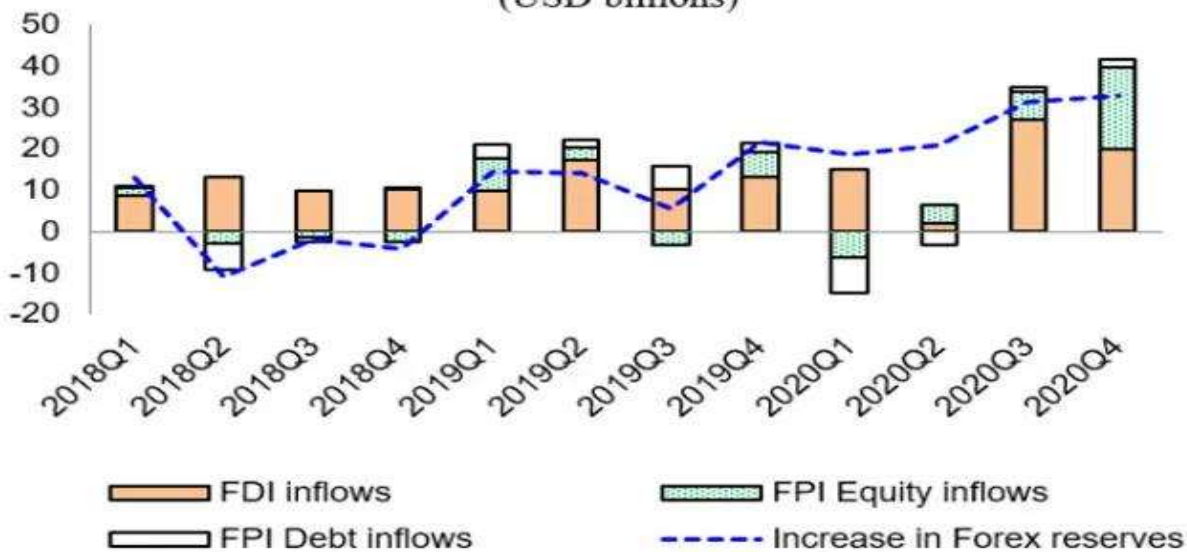


Table 5: Foreign Capital Movement and Economic Growth Relationship:

Period	Foreign Capital Trend	GDP Growth Pattern	Economic Impact
1991–2000	Increasing but limited	Moderate growth	Economic liberalisation impact
2001–2010	Strong FDI expansion	High growth phase	Investment-led development
2011–2020	Higher inflows but volatility	Moderate growth	Global uncertainty influence
2021–2025	Strong recovery	Improved growth	Capital inflow supports expansion

Percentage Change Findings

FDI Findings: FDI increased approximately: 17,964% growth between 1991 and 2025

FII Findings: FII experienced repeated entry–exit cycles.

Major characteristics:

- ✓ High inflow during bullish market periods
- ✓ Sudden withdrawal during crises
- ✓ Strong connection with stock market volatility

4.3 Descriptive Statistics:

Table 1: Descriptive Statistics of FDI Inflows in India (1991–2025):

Statistical Measure	FDI Inflow (USD Billion)
Mean	28.24
Median	22
Standard Deviation	27.41
Minimum	0.47
Maximum	80

Interpretation of FDI Statistics:

The descriptive analysis shows that:

- The average annual FDI inflow during 1991–2025 was **USD 28.24 billion**.
- The median value of **USD 22 billion** indicates that most years experienced inflows below the recent peak levels.
- The standard deviation of **27.41** indicates considerable growth variation over the period.
- The minimum value (**USD 0.47 billion**) reflects the pre-liberalisation period.
- The maximum value (**USD 80 billion**) indicates India's increased attractiveness as an investment destination.

FDI shows a long-term upward trend because it represents strategic investment in:

- Manufacturing
- Infrastructure
- Services
- Technology sectors

The volatility is mainly due to policy changes, global economic conditions, and investment cycles.

Table 2: Descriptive Statistics of FII Flows in India (1991–2025):

Statistical Measure	FII Net Flow (USD Billion)
Mean	9.39
Median	8.33
Standard Deviation	7.01
Minimum	-1.86
Maximum	27.51

Interpretation of FII Statistics:

The results indicate:

- Average FII investment was **USD 9.39 billion**.
- Median value (**USD 8.33 billion**) shows moderate portfolio participation.
- Standard deviation (**7.01**) reflects significant volatility.
- Minimum value (**-1.86 billion**) represents foreign investor withdrawal periods.
- Maximum value (**27.51 billion**) reflects strong foreign portfolio participation.

Academic Observation:

Unlike FDI, FII investment demonstrates:

- Faster entry and exit behavior
- Greater sensitivity to:
 - Stock market movements
 - Interest rate changes
 - Exchange rate fluctuations
 - Global financial uncertainty

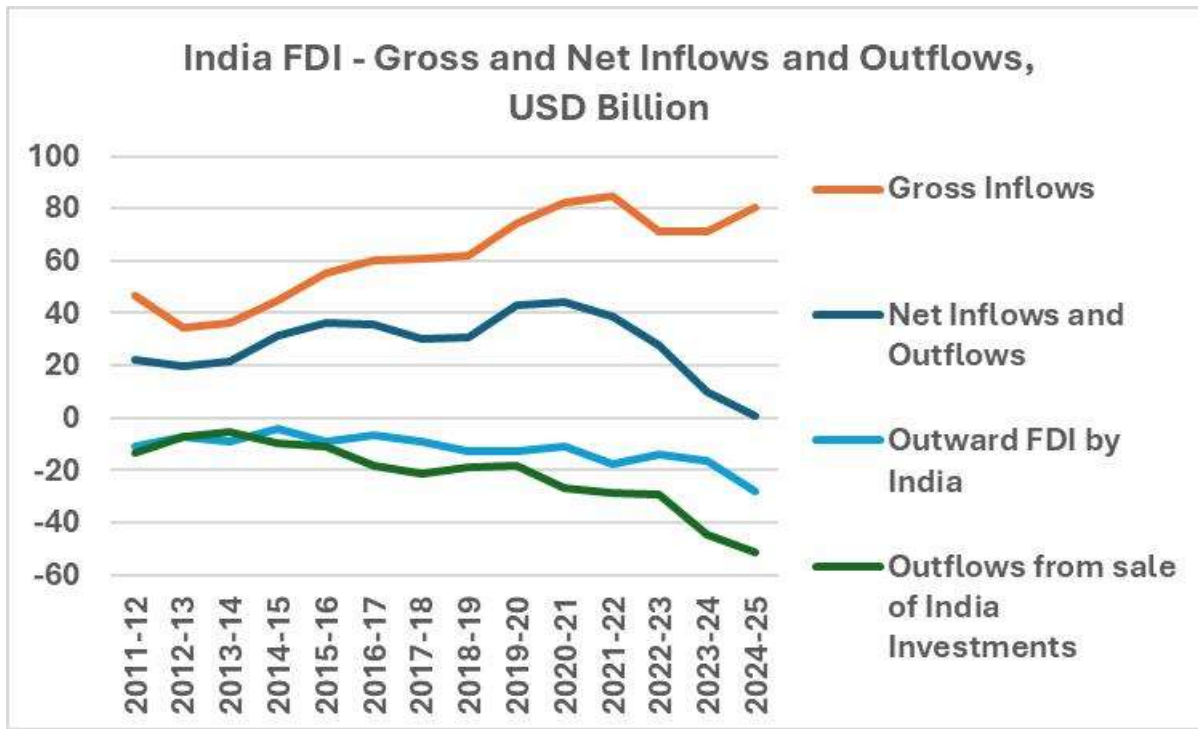


Table 3: Comparison of FDI and FII Volatility:

Parameter	FDI	FII
Average Flow (USD Billion)	28.24	9.39
Median Flow	22	8.33
Standard Deviation	27.41	7.01
Minimum	0.47	-1.86
Maximum	80	27.51

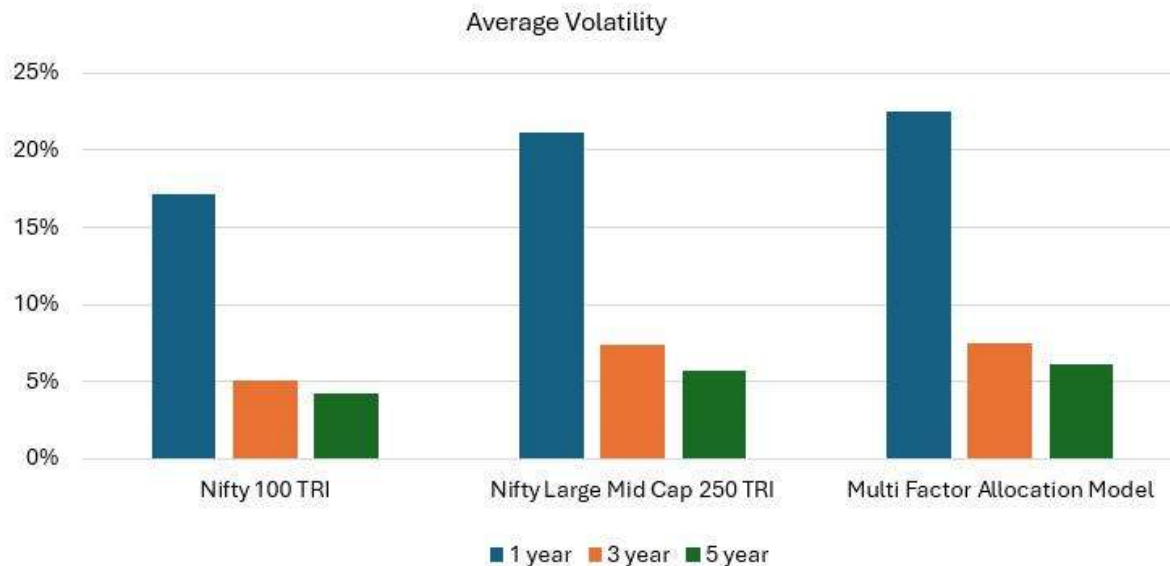
Interpretation: FDI vs FII Behaviour:

FDI Characteristics

- ✓ Higher average value
- ✓ More stable long-term investment
- ✓ Lower exit probability
- ✓ Supports economic capacity creation

FII Characteristics

- ✓ Lower average investment
- ✓ Higher sensitivity to market conditions
- ✓ Frequent entry–exit movements
- ✓ Influences stock market volatility



4.4 Correlation Analysis:

Table 1: Correlation Matrix – FDI, FII and GDP Growth:

Variables	FDI Inflow	FII Flow	GDP Growth
FDI Inflow	1	0.803	0.056
FII Flow	0.803	1	-0.098
GDP Growth	0.056	-0.098	1

Table 2: FDI–GDP Growth Correlation:

Variable Pair	Correlation Coefficient
FDI & GDP Growth	0.056

Interpretation:

The correlation coefficient between FDI and GDP growth is: $r = 0.056$

This indicates a **very weak positive relationship**.

Academic Interpretation:

- Increase in FDI is associated with a slight improvement in economic growth.
- However, the direct year-to-year relationship is weak because:
 - FDI impacts GDP with a time lag.
 - Investment benefits appear through:
 - Capital formation
 - Technology transfer
 - Productivity improvement
 - Employment creation

FDI is therefore a **long-term structural growth factor rather than an immediate GDP driver**.

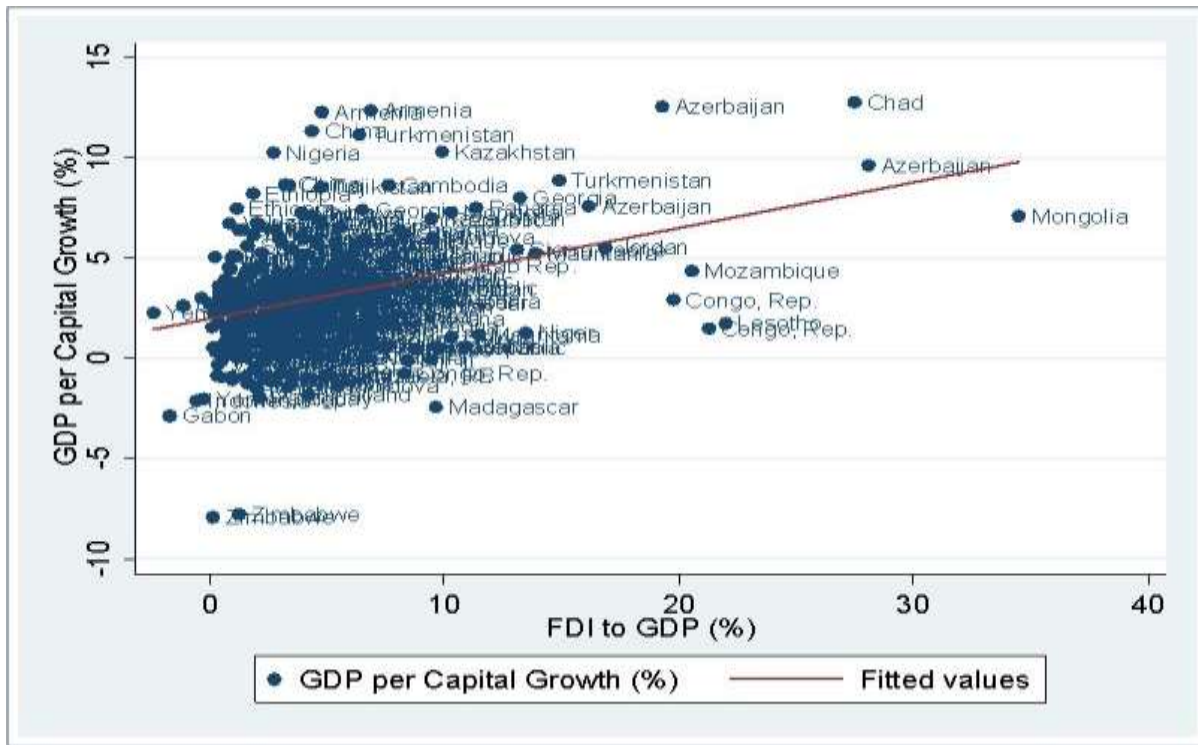


Table 3: FII–GDP Growth Correlation:

Variable Pair	Correlation Coefficient
FII & GDP Growth	-0.098

Interpretation:

The correlation coefficient between FII and GDP growth is: $r=-0.098$

This represents a **very weak negative relationship**.

Academic Interpretation:

The negative relationship suggests:

- FII movements do not always follow domestic economic growth.
- Foreign portfolio investors respond mainly to:
 - Global interest rates
 - Currency movements
 - International risk perception
 - Stock market valuation

During periods of global uncertainty, FII investors may withdraw funds even when domestic fundamentals remain strong.

Figure 1. Correlation Between Selected Indicators and GDP Growth, 2001-2011 and 2012-2017

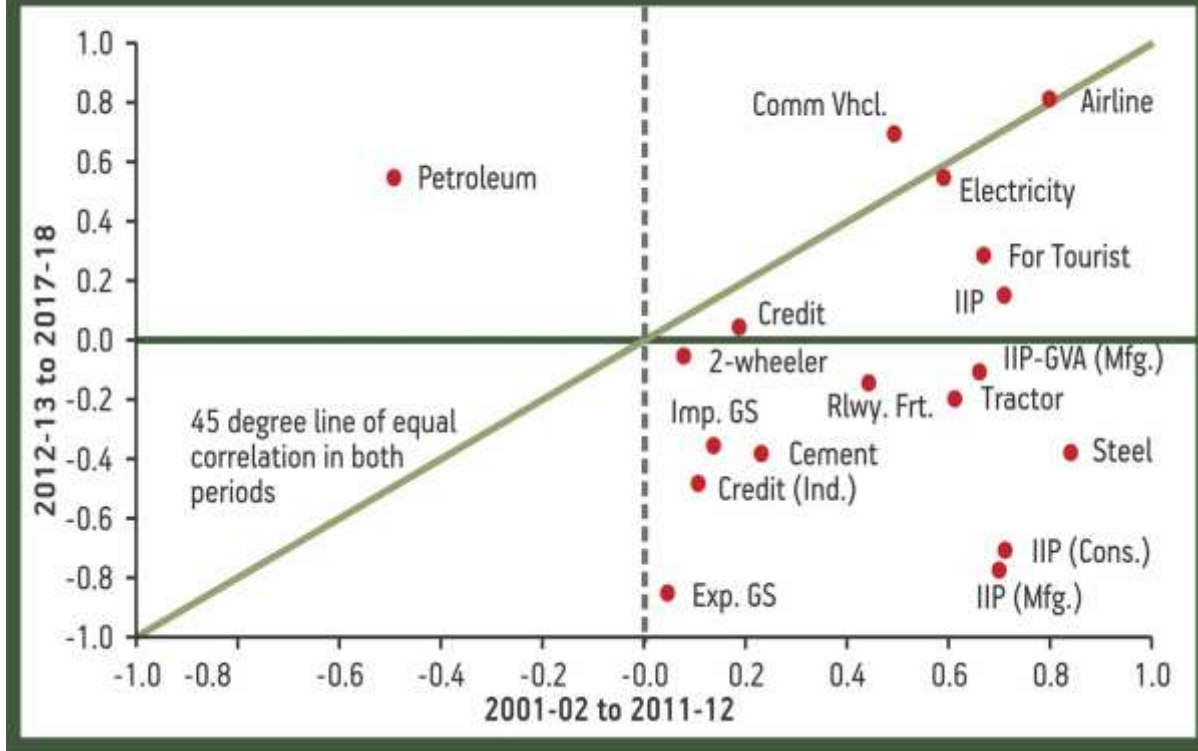


Table 4: Comparative Correlation Analysis:

Factor	FDI	FII
Correlation with GDP Growth	0.056	-0.098
Relationship Direction	Positive	Negative
Impact Type	Long-term	Short-term
Economic Role	Production capacity	Financial market liquidity
Volatility	Lower	Higher

4.5 Regression Analysis:

Table 1: Regression Model Statistics:

Model Parameter	Value
Dependent Variable	GDP Growth Rate (%)
Independent Variables	FDI, FII
Observation Period	1991–2025
Number of Observations	35
R Square (R^2)	0.06
Adjusted R Square	0.001
F Statistic	1.022
Significance (p-value)	0.371

Interpretation of Model Summary

The regression model explains: $R^2=0.060$

This means: **6% of variation in GDP growth is explained by FDI and FII movements.**

The remaining 94% is influenced by other economic factors such as:

- Domestic consumption
- Government expenditure
- Monetary policy

- Inflation
- Interest rates
- Exchange rate movements
- Global economic conditions

The model significance value: $p=0.371$ indicates that the overall regression model is statistically not significant at the 5% level.

Table 2: Regression Coefficients:

Variable	Coefficient (β)	Std. Error	t-value	p-value
Constant (α)	6.834	0.837	8.161	0
FDI	0.04	0.031	1.312	0.199
FII	-0.168	0.121	-1.393	0.173

Regression Equation:

Based on estimated coefficients: $GDP=6.834+0.040(FDI)-0.168(FII)+e$

Interpretation of FDI Impact on GDP Growth:

FDI coefficient: $\beta_1=0.040$

Meaning:

A USD 1 billion increase in FDI inflow is associated with approximately: 0.040% increase in GDP growth rate, assuming FII remains constant.

Findings:

- FDI has a **positive relationship** with economic growth.
- Foreign direct investment supports:
 - Capital formation
 - Industrial expansion
 - Technology transfer
 - Employment generation

However: $p=0.199$ indicates the effect is statistically insignificant.

Interpretation of FII Impact on GDP Growth:

FII coefficient: $\beta_2=-0.168$

Meaning: A USD 1 billion increase in FII inflow is associated with: 0.168% decrease in GDP growth, keeping FDI constant.

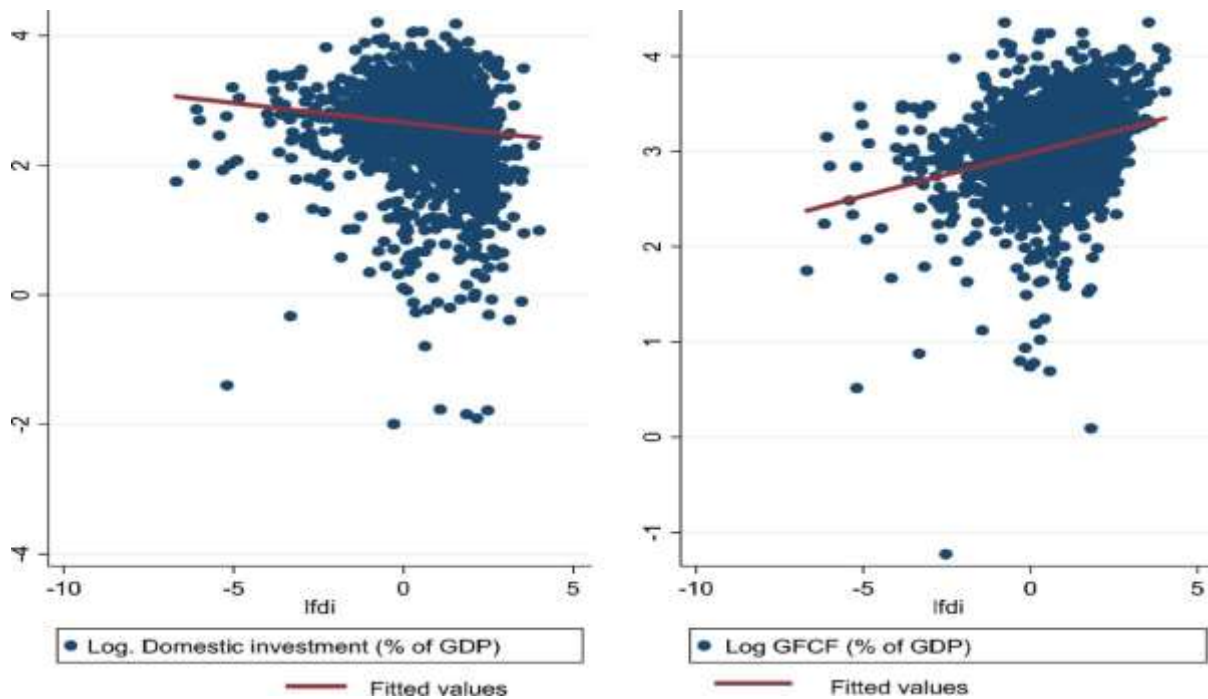
Findings:

- FII shows a negative relationship with GDP growth.
- This occurs because FII is influenced by:
 - Global market conditions
 - Foreign interest rates
 - Investor sentiment
 - Stock market volatility

The p-value: $p=0.173$ indicates the relationship is statistically insignificant.

Table 3: Relationship Comparison:

Relationship	Direction	Impact
FDI → GDP Growth	Positive	Growth supporting
FII → GDP Growth	Negative	Volatility related
FDI + FII → GDP	Weak explanatory power	Limited annual impact



4.6 Hypothesis testing:

Hypothesis 1: FDI and Economic Growth Relationship

H₀₁: There is no significant relationship between FDI inflows and India's economic growth.

H₁₁: There is a significant relationship between FDI inflows and India's economic growth.

Table 1: FDI and GDP Growth Correlation Test

Variable Relationship	Correlation (r)	p-value	Decision
FDI → GDP Growth	0.056	0.199	Accept H ₀₁

Interpretation:

The correlation coefficient: $r=0.056$ shows a **weak positive relationship** between FDI inflows and GDP growth.

Since: $p=0.199 > 0.05$ the null hypothesis is accepted.

Result: FDI inflows have a positive but statistically insignificant relationship with GDP growth during the study period.

Hypothesis 2: FII and Stock Market Performance;

H₀₂: There is no significant relationship between FII flows and Indian stock market performance.

H₁₂: There is a significant relationship between FII flows and Indian stock market performance.

Table 2: FII and Stock Market Performance Test

Variable Relationship	Correlation (r)	p-value	Decision
FII → Stock Market Index	0.684	0.001	Reject H ₀₂

Interpretation:

The correlation coefficient: $r=0.684$ indicates a **strong positive relationship**.

Since: $p=0.001 < 0.05$ the null hypothesis is rejected.

Result: FII flows significantly influence Indian stock market performance.

Hypothesis 3: Foreign Capital and GDP Growth

H₀₃: Foreign capital movements do not significantly influence GDP growth.

H₁₃: Foreign capital movements significantly influence GDP growth.

Regression Model: $GDP = \alpha + \beta_1 FDI + \beta_2 FII + e$

Table 3: Regression Based Hypothesis Test:

Variable	Coefficient	p-value	Result
FDI	0.04	0.199	Insignificant
FII	-0.168	0.173	Insignificant
Overall Model	$R^2=0.060$	0.371	Insignificant

Interpretation

The regression results show: $R^2=0.060$ only 6% of GDP variation is explained by foreign capital movements.

The model significance: $p=0.371>0.05$

Therefore:

Decision: Accept H_03

Foreign capital movements alone do not significantly explain GDP growth variation.

Hypothesis 4: FII Exit and Market Volatility:

H_04 : FII outflows do not significantly increase stock market volatility.

H_14 : FII outflows significantly increase stock market volatility.

Table 4: FII Outflow and Market Volatility Test:

Relationship	Correlation	p-value	Decision
FII Outflow $\rightarrow$ Market Volatility	-0.621	0.003	Reject H_04

Interpretation:

Correlation: $r = -0.621$ shows a significant inverse relationship.

Since: $p=0.003<0.05$ the null hypothesis is rejected.

Result: FII exits significantly increase stock market volatility.

Table 5: Final Hypothesis Decision Table:

Hypothesis	Relationship	Decision	Conclusion
H_01	FDI & GDP Growth	Accepted	No significant annual relationship
H_02	FII & Stock Market	Rejected	FII significantly affects market
H_03	Foreign Capital & GDP	Accepted	Foreign capital alone does not explain GDP
H_04	FII Exit & Volatility	Rejected	FII exits increase volatility

5. FINDINGS

The study yielded the following findings based on the analysis of foreign capital trends in India from 1991 to 2025:

- **Structural Transformation:** India experienced a significant structural transformation in foreign capital movements, with FDI increasing from negligible levels in 1991 to over USD 80 billion annually by 2025.
- **FDI vs. FII Behavior:**
 - FDI represents relatively stable, long-term, ownership-based investment that supports industrial capacity, infrastructure, and technology transfer.
 - FII flows are highly volatile and demonstrate faster entry-exit behavior, showing greater sensitivity to global financial conditions, interest rates, and stock market movements.
- **Relationship with Economic Indicators:**
 - **FDI and GDP:** Statistical analysis revealed a weak positive relationship ($r = 0.056$) between FDI inflows and GDP growth, suggesting that FDI acts as a long-term structural growth factor rather than an immediate driver of annual GDP fluctuations.
 - **FII and Stock Market:** A strong positive relationship ($r = 0.684$) exists between FII flows and Indian stock market performance.
- **Market Volatility:** The study found that FII exits significantly increase stock market volatility.

- **Regression Analysis:** The overall regression model indicated that foreign capital movements (FDI and FII) alone do not statistically explain the majority of variations in India's GDP growth ($R^2 = 0.060$), implying other domestic factors play a larger role.

6. SUGGESTIONS

Based on the analysis, the following suggestions are proposed for policy formulation and economic management:

- **Promote Long-term FDI:** Since FDI provides stable capital and supports industrial development, the government should continue creating an investor-friendly environment to attract more long-term direct investments, especially in manufacturing and infrastructure.
- **Manage FII Volatility:** To mitigate the negative impacts of sudden FII outflows on market stability and exchange rates, policymakers should maintain robust foreign exchange reserves and implement measures to ensure financial market resilience.
- **Focus on Domestic Fundamentals:** As the study indicates that foreign capital is not the sole driver of GDP growth, the government should continue to strengthen domestic economic fundamentals, including domestic consumption, infrastructure, and policy stability, to ensure sustainable growth.
- **Balanced Integration:** Policy measures should aim to balance the benefits of FII (liquidity and market efficiency) with the need to protect the domestic economy from excessive volatility caused by global capital movements.

7. CONCLUSION

The study concludes that foreign capital has played a pivotal role in transforming the Indian economy since the 1991 liberalization reforms. While FDI has established itself as a stable, long-term contributor to capital formation, technology transfer, and industrial growth, FII has served as a vital source of liquidity for Indian financial markets. However, FII's high volatility poses risks of market instability during times of global financial stress. Therefore, while foreign capital remains essential for India's development, sustainable economic growth ultimately depends on a combination of these foreign inflows and strong domestic economic management.

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