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**ATTACHMENT BETWEEN STOCK INDICES FII, NSE AND BSE**

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**ABSTRACT**

*The aim of this study is to identify the relationship between the Foreign Institutional Investment inflows and stock indices of India. In this context, an empirical study was conducted. The period of 1999-2009 is taken to analyze the correlation between BSE index and FII inflows and the period 2003-2009 is taken to know the relation between NSE index and FII inflows. It is found that there is a significant positive correlation between the BSE index and the FII inflows and the NSE index and FII inflows.*

**KEYWORDS**

stock indices, FII, NSE, BSE.

**INTRODUCTION**

Foreign Institutional investors have played a major role in the emergence of truly money flows, notably through their cross-border investments. India has become the most attractive destination and was placed at the second spot in the year 2008 by the Global Retail Development Index. Thus, the foreign institutional investors have gained a significant role in the Indian Capital markets. Many overseas institutional investors, especially those from Europe and the US, almost always purchase stocks on the basis of fundamentals. Further, stock price movements correspond to the activities of foreign institutional investors. However, another concern of investors regards conditions other than the actual purchase of stocks. This paper examines the relationship between movements of Foreign Institutional Investment (FII) inflows and stock indices of India. The period of 1999-2009 is taken to analyze the correlation between BSE index and FII and the period 2003-2009 is taken to know the relation between NSE index and FII. It is found that there is a significant positive correlation between the BSE index and the FII inflows and the NSE index and FII inflows.

**STATEMENT OF THE PROBLEM****STOCK MARKET PERFORMANCE**

Stock Market performance is an indicator of the overall health of the economy. If the general perception of investor about the economic performance is negative, the stock market gets decline and showing a bearish trend. At the same time, if the investor's perception is positive then the stock market performance is also good and bull markets are inevitable. Hence, overall economic and stock specific performance influences performance of the market. Thus, Stock Market Performance acts as the barometer of the economy as a whole.

**FOREIGN INSTITUTIONAL INVESTMENT**

The World Bank is advised to the developing countries to develop their stock markets to get foreign private capital flows in form of foreign institutional investors. It was suggested that these investments would help the stock markets directly through widening investor foundation and indirectly gripping the local authorities to improve the trading system. While the volatility associated with the foreign institutional investor's investment strategies is well known, there was also concern that foreign institutional investors might introduce distortion in the host country markets due to pressure on them to secure capital gains. Thus, it becomes important to assess the impact of foreign institutional investors on the Indian stock exchange.

**LITERATURE REVIEW**

Considerable amount of research have been conducted about the impact of financial and macroeconomic variables on stock prices in different economies with widespread econometric methods. Suchismita Bose and Dipankor Coondoo (2004) investigated the impacts of reforms of the foreign institutional investors' investment policy, on FII portfolio flows to the Indian stock markets and found that the policies mostly render FII investments more sensitive to the domestic market returns. Fama (1981) said that the stock prices reflect these variables such as inflation, exchange rate, interest rate and industrial production. Later Maysami and Koh (2000) and Choi et al (1992) examined the impacts of the interest rate and exchange rate on the stock returns and showed that the exchange rate and interest rate are the determinants in the stock prices. Frank and Young (1972) investigated the relationship between stock prices and exchange rates by employing six different exchange rates and concluded no statistically significant underlying relationship between the two. Rajesh Chakrabati (2001) analyze these flows and their relationship with other economic variables and concluded that the equity flows are highly correlated with equity returns in India, they are more likely to be the effect than the cause of these returns. Kishor C. Samal (1997) investigated the main features of India's equity market and its consequent problems due to the hot money movement by Foreign Institutional investors (FIIs) and concluded that there has been increased liberalization of domestic financial and capital markets. Nidhi Dhamija (2008) examines the role of various factors relating to individual firm-level characteristics and macroeconomic-level conditions influencing FII investment and the study revealed regulatory environment of the host country has an important impact on FII inflows and the pace of foreign investment began to accelerate, regulatory policies have changed to keep up with changed domestic scenarios. P.Krishna Prasanna (2008) examined the contribution of foreign institutional investment particularly among companies included in sensitivity index (Sensindex) of Bombay Stock Exchange and also examined the relationship between Foreign institutional investment and firm specific characteristics and . It is observed that foreign investors invested more in companies with a higher volume of shares owned by the general public. Douma, Pallathiatta and Kabir (2006) investigated the impact of foreign institutional investment on the performance of emerging market firms and found that there is positive effect of foreign ownership on firm performance. They also found impact of foreign investment on the business group affiliation of firms. Aggarwal, Klapper and Wysocki (2005) observed that foreign investors preferred the companies with better corporate governance. Investor protection is poor in case of firms with controlling shareholders who have ability to expropriate assets. The block shareholders affect the value of the firm and influence the private benefits they receive from the firm. Companies with such shareholders will find it expensive to raise external funds. Yin-Hua and Woidtke (2005) found that when company boards are dominated by members who are affiliated to the controlling family, investor protection will be relatively weak and it is difficult to determine the degree of separation of management from ownership. They also observed that firm value is negatively related to board affiliation in family controlled firms. Li (2005) observed that in case of poor corporate governance the foreign investors choose foreign direct investment (FDI) rather than indirect portfolio investment. It is generally believed that FDI could be better protected by private means. Aswani Kumar Bhalla (2008) analyzed the India's growth story in the terms of real welfare of the people, the role of foreign institutional investment in India and found the governments are following similar policy measures to attract foreign investment in India to correct both their fiscal failures, balance of payments and to increase foreign exchange reserves in the name of giving the boost to the economy.

**OBJECTIVES AND HYPOTHESIS**

- **PRIMARY OBJECTIVE**

1. To study the relationship between the performance of stock markets and Foreign Institutional Investment inflows in India.

• **SECONDARY OBJECTIVES**

1. To study the relationship between the performance of Bombay stock market and the foreign institutional investment inflows.
2. To study the relationship between the performance of National Stock Market and the foreign institutional investment inflows.
3. To study the relationship between the performance of National stock exchange, Bombay stock exchange and FII inflows.

**HYPOTHESIS**

1. **H<sub>0</sub>**: There is no significant relationship between BSE market performance and FII inflows in India.
2. **H<sub>0</sub>**: There is no significant relationship between NSE market performance and FII Inflows in India.
3. **H<sub>0</sub>**: There is no significant relationship between NSE, BSE markets performance and FII Inflows in India.

**METHODOLOGY**

Research Design is Analytical in nature. The study is undertaken for a period of 11 years from January 1999 to December 2009 to assess the relationship between BSE performance and FII inflows and a period of 7 years from January 2003 to December 2009 to know the relationship between NSE performance and FII inflows. Sample size is 360 for each sample element, the sample frequency being monthly.

The entire data set is secondary data collected from the following websites:

1. <http://www.moneycontrol.com> , a web-site of database is compiled on the basis of reports submitted to SEBI by custodians and constitutes trades conducted by FII.
2. <http://finance.yahoo.com>, providing historical data pertaining to stock market indices.

Correlation technique is used for analysis (a perfect correlation is represented by a correlation coefficient of 1; perfect negative correlation by -1 and zero represents no correlation), ANOVA is used to analyze the relationship among the BSE, NSE and FII inflows in India and bar charts are used for pictorial representations of the relationships.

**ANALYSIS AND FINDINGS**

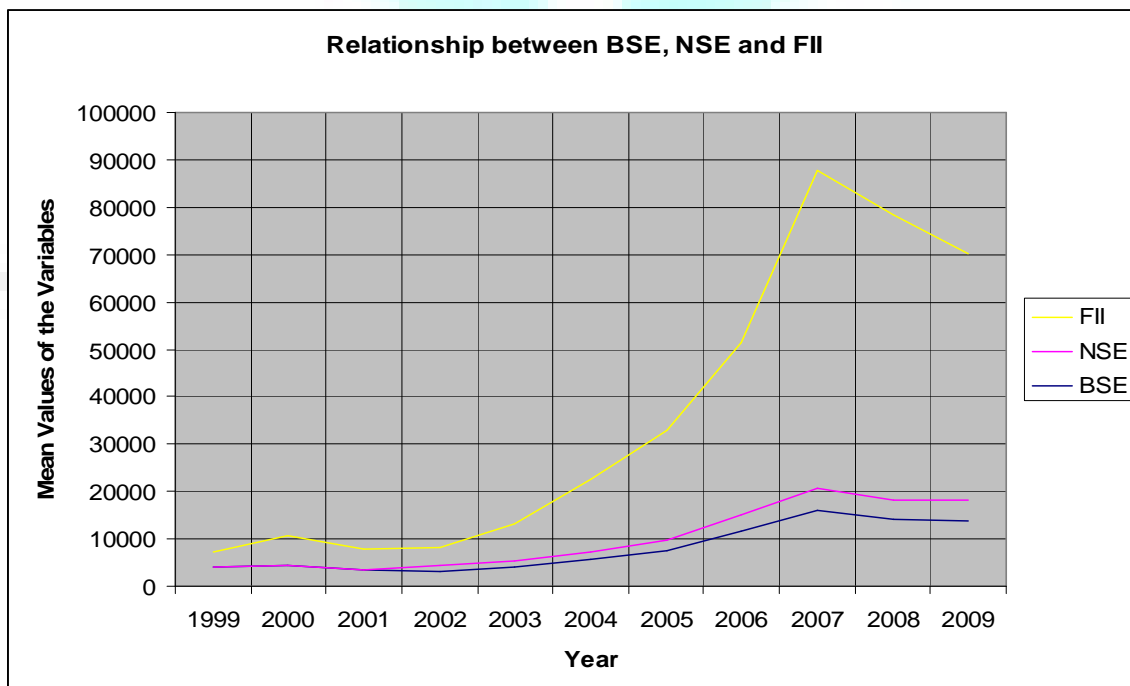
**PERFORMANCE OF STOCK MARKETS AND FII**

Table No.1 shows the descriptive statistics of the variables. From this table, the mean value of FII increases, the other variables (NSE and BSE) also increases. And also shows the interrelationship between BSE, NSE and FII Inflows in India. Almost all the variables move in the same direction.

**TABLE NO. 1: DESCRIPTIVE STATISTICS FOR VARIABLES**

Year	Mean			Std. Deviation		
	BSE	NSE	FII	BSE	NSE	FII
1999	4166.62		3032.958	642.9509		978.1156
2000	4501.888		6232.625	531.5		1844.524
2001	3475.922		4322.217	446.7641		1614.59
2002	3230.578	1013.67	3860.026	194.376	59.39326	809.8928
2003	3967.638	1264.071	7901.375	928.3005	299.8477	3854.661
2004	5551.601	1751.35	15323.64	531.4195	171.2462	3131.453
2005	7498.368	2297.104	23182.18	1038.343	284.7412	5434.226
2006	11647.7	3425.871	36317.03	1328.131	335.3277	8584.2
2007	15901.44	4680.646	67097.3	2640.503	829.6906	23533.04
2008	14028.76	4198.833	60063.15	3137.13	909.3233	20420.82
2009	13941.48	4183.446	52167.04	3195.1	901.83	18302.02
<b>TOTAL</b>	<b>7992</b>	<b>2996.452</b>	<b>25409.05</b>	<b>4966.922</b>	<b>1429.076</b>	<b>25833.76</b>

**CHAT NO.1**



Chat No.1 shows the relationship between BSE, NSE and FII inflows in India. This shows the significant relationships between the variables. The BSE and NSE index move along with the FII Inflows.



**HYPOTHESIS TESTING**

**H<sub>0</sub>:** There is no significant relationship between BSE market performance and FII inflows in India.

Table 2 shows that the calculated value of significance (0.000) is less than the assumed significance value (0.01) and hence the null hypothesis is rejected and alternative hypothesis is accepted. There is a positive significant relationship between BSE market performance and FII Inflows in India.

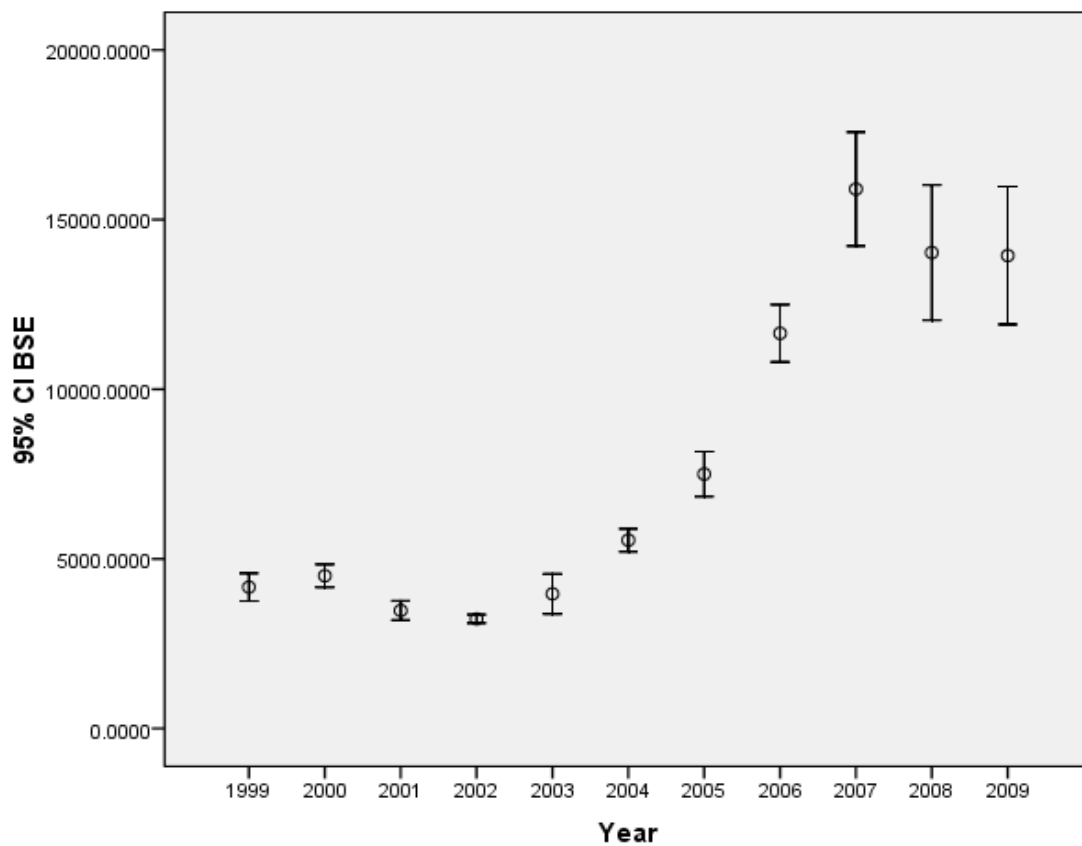
**TABLE 2: TESTING OF HYPOTHESIS  
CORRELATIONS**

		FII	BSE
FII	Pearson Correlation	1	.947**
	Sig. (2-tailed)		.000
	N	132	132
BSE	Pearson Correlation	.947**	1
	Sig. (2-tailed)	.000	
	N	132	132

\*\* . Correlation is significant at the 0.01 level (2-tailed).

**H<sub>0</sub>:** There is no significant relationship between NSE market performance and FII inflows in India.

Table 3 shows that the calculated value of significance (0.000) is less than the assumed significance value (0.01) and hence the null hypothesis is rejected and alternative hypothesis is accepted. There is a significant relationship between NSE market performance and FII Inflows in India.



The error bar chart of figure 1 shows that the error bars for the years 2004 and 2005 do not overlap. This shows that there is no a significant relationship between the performance of BSE in the year 2003 and 2004. The BSE Indices are highly correlated in the rest of the years.

**TABLE 3: TESTING OF HYPOTHESIS  
CORRELATIONS**

		NSE	FII
NSE	Pearson Correlation	1	.928**
	Sig. (2-tailed)		.000
	N	89	89
FII	Pearson Correlation	.928**	1
	Sig. (2-tailed)	.000	
	N	89	89

\*\* . Correlation is significant at the 0.01 level (2-tailed).

**H<sub>0</sub>:** There is no significant relationship between BSE, NSE markets performance and FII inflows in India.

Table 4 shows that the calculated value of significance (0.000) is less than the assumed significance value (0.01) and hence the null hypothesis is rejected and alternative hypothesis is accepted. There is a noteworthy relationship between BSE, NSE markets performance and FII Inflows in India, which is the same as concluded from the previous analysis.

TABLE: 4 TESTING OF HYPOTHESIS

ANOVA Table		Sum of Squares	df	Mean Square	F	Sig.
FII * date	Between Groups (Combined)	7.157E10	10	7.157E9	54.625	.000
	Within Groups	1.585E10	121	1.310E8		
	Total	8.743E10	131			
BSE * date	Between Groups (Combined)	2.880E9	10	2.880E8	99.195	.000
	Within Groups	3.514E8	121	2903818.350		
	Total	3.232E9	131			
NSE * date	Between Groups (Combined)	1.507E8	7	2.152E7	59.970	.000
	Within Groups	2.907E7	81	358870.453		
	Total	1.797E8	88			

## CONCLUSION

Foreign Institutional Inflows effect varies from country to country. It can affect the productivity and balance of payment of the recipient country. But, in developing countries have been a great need for foreign capital to increase the productivity and to build up foreign exchange reserves to meet the current account deficit. Thus, foreign investment provides a way to get foreign capital.

A more investment by FIIs indicates that they are confident in Indian market. These Foreign institutional investors are highly influence the stock market performance. The sub-prime crisis and other economic conditions had caused a liquidity crunch for these institutions, so they are forced to withdraw money from Indian market so as to repay loans they had taken. These withdrawals had caused panic in Indian stock market. It is required to understand when they withdraw their funds? And when they invest more money?. Because there is a high positive correlation between stock market performance and FII inflows in India.

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