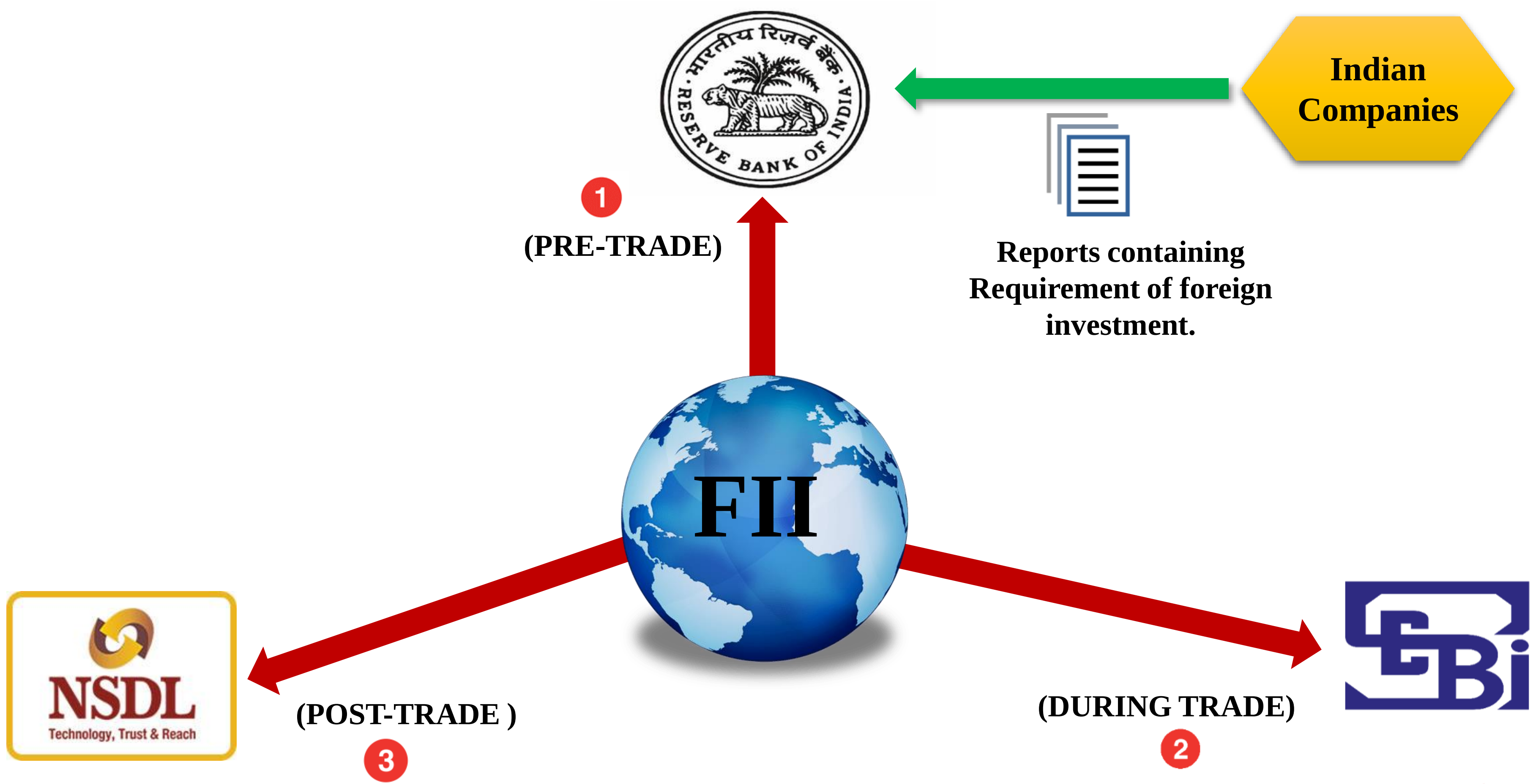
Foreign Portfolio Investment



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FPI in India or FII

- The depositories – NSDL and CDSL- are required to maintain the data on FPIs
- FPI stands for those investors who hold a short term view on the company, in contrast to Foreign Direct Investors (FDI)
- FPIs generally participate through the stock markets and gets in and out of a particular stock at much faster frequencies
- 1% up to 100 % * (visit RBI)

FII/FPI	No
Category 1	269
Category 2	7795
Category 3	1160
Total FII/FPI	**9224**

Categories of FPI

As part of Risk based approach towards customer identity verification (KYC), FPIs have been categorized into three major categories:

- **Category I (Low Risk)** which would include Government and entities like Foreign Central banks, Sovereign wealth Funds, Multilateral Organizations, etc
- **Category II (Moderate Risk)** which would include Regulated entities such as banks, Pension Funds, Insurance Companies, Mutual Funds, Investment Trusts, Asset Management Companies, University related endowments (already registered with SEBI)
- **Category III (High Risk)** which would include all other FPIs not eligible to be included in the above two categories

Statistics - FII

Financial Year	INR crores		
	Equity	Debt	Total (INR CR)
2008-09	-47,706.00	1,895.00	-45,811.00
2009-10	1,10,221.00	32,438.00	1,42,658.00
2010-11	1,10,121.00	36,317.00	1,46,438.00
2011-12	43,738.00	49,988.00	93,726.00
2012-13	1,40,033.00	28,334.00	1,68,367.00
2013-14	79,709.00	-28,060.00	51,649.00
2014-15	1,11,333.00	1,66,127.00	2,77,461.00
2015-16	-14,172.00	-4,004.00	-18,176.00
2016-17	55,703.00	-7,292.00	48,411.00
2017-18	25,635.00	1,19,036.00	1,44,682.00
2018-19 **	-21,051.00	-43,684.00	-64,852.00
Total is from 1992-1993	**8,65,538.00**	**3,70,590.00**	**12,36,019.00**

Red Flag (< 3%) Vs Breach

					Overall / Sectoral Limit		
Sr No.	Issuer / Company Name	ISIN	ISIN Description	Security Type	Aggregate Investment (%)	Aggregate Permissible Limit (%)	Available Investment Headroom (in terms of Quantity)
1	HDFC BANK LIMITED	INE040A01026	HDFC BANK LIMITED EQ NEW RS. 2/-	Equity	72.56	74	39,037,825
2	NOVARTIS (INDIA) LIMITED	INE234A01025	NOVARTIS INDIA LIMITED EQ FV RS.5	Equity	71.25	74	678,877

Geographic Breakdown

Regions | **Top Countries**

Japan	12.3%
United Kingdom	11.3%
China	9.1%
India	7.4%
France	7.1%
South Korea	4.9%
Hong Kong	4.5%
Canada	3.6%
Germany	3.2%
Netherlands	3.0%

Percentage of net assets as of 6/30/2018 (updated quarterly)

CAPITAL GROUP

- This $164 billion fund owns roughly Rs 80,000 crore worth of Indian shares, making it the largest foreign portfolio investor (FPI) in India

- Private lender HDFC Bank (fourth), Reliance Industries NSE -0.53 % (sixth), Kotak Mahindra's 0.95 % Bank (14th) are a few Indian stocks, which were among its top 25 holdings in value terms as of June 30

- A part of American Funds, owned by investment management firm Capital Group, this is Euro Pacific Growth Fund

Participatory Notes in India: The Self-Destructive Route

How PN Functions

USA Investor

↓ Buy X Shares ↑

USA Broking House

↓ Buy X Shares ↑

Indian broking house

Buy X Shares

↓ **X Shares (India)** ↑

Issues PN with X shares as Underlying assets

Confirmation of shares purchased

Participatory Notes

- **Participatory Notes** commonly known as **P-Notes** or **PNs** are instruments issued by registered foreign institutional investors (FII) to overseas investors, who wish to invest in the Indian stock markets without registering themselves with the market regulator, the Securities and Exchange Board of India - SEBI
- SEBI permitted foreign institutional investors to register and participate in the Indian stock market in 1992
- The absolute value of P-Notes investments rose to a record of Rs 4.5 lakh crore in October 2007
- However, mainly due to SEBI's strengthening of the regulatory framework for P-notes, their investments fell to a record low of Rs **80,341 crore** . The amount of Foreign Portfolio Investments (FPI) via P-Notes decreased from a high of 55% (October 2007) to 2.4% (Aug 2018)

PROBLEMS

1. **Multi layering** enables the original investor to invest in financial markets by hiding his/her identity through multiple layers of investment activity before investing in a financial market.

A high-profile case in 2009 involved the Reliance ADAG group that was alleged to have manipulated the shares of Reliance Communication through a multi-layered transaction involving shell companies, PNotes and prominent international investment banks

2. Round-tripping is the process by which tax-free illicit or black money leaves India through illegal routes, and is then repatriated to the country with minimal fees.

In the context of black money, it leaves the country through various channels such as inflated invoices, payments to shell companies overseas, the hawala route and so on.

PROBLEMS

3.Hedge Funds

4. Terror Financing

5. Volatility through outflows

Financial Year	Notional Value of PNs (A) (in crores)	Total FII value (B) (in crores)	A as percentage of B
2003-2004	15726.75	78618.25	20.00%
2004-2005	44641.5	182784	24.42%
2005-2006	85187.9	323668	26.31%
2006-2007	167703.9	493858.4	33.95%
2007-2008	348375.5	785554.8	44.34%
2008-2009	130387.8	537449.6	24.26%

Ketan Parekh Scam, 2001.

ı Parekh-led stock market scam of 2001
$2 billion had been brought in and taken out of
seas corporate bodies) registered in Mauritius

h foreign-based PN holders and he used PNs for
es. Shares like Visual soft rose from Rs. 625 to Rs.
ftware from Rs. 90 to Rs. 2,150

- Thus, PNs are susceptible to abuse. It was only after these revelations that SEBI barred the issuing of PNs to any unregulated entities and also enforced certain disclosures about PNs

“Black Monday” crash in May, 2004

- In May, 2004 Sensex crashed by 842 points. SEBI unmasked the culprit behind this crash. It was none other than PNs
- UBS, one of the largest sellers of shares, carried out large scale selling orders on behalf of unidentified clients
- These clients transacted in Indian stocks through UBS, but hid behind a maze of investment deals extending all the way from India to Mauritius
- What happened in 2004 was a double whammy. Not only were markets bought down through artificial selling pressure, but Indians invested in stocks via a route (the PN route) reserved only for foreign investors
- It could be inferred that a large fraction of foreign institutional investment is not really foreign. It is Indian money circulating around the world and re-entering the country as foreign money all illegal

P-Note Crisis, 2007

- The notorious nature of P-Notes coerced SEBI to introduce certain restrictions which curbed the freedom of PN holders

- However, the guidelines of SEBI were vague and this propelled the biggest intra-day collapse in Indian stock markets – Sensex crashed by 1744 points or about 9% of its value

New Rules by SEBI

- Know your client
- GAAR – General Anti-Avoidance Rule (India)
- Tobin Tax (STT)

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THANK YOU

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