Mains Marathon

Day 15: What is the difference between FDI and FPI? How does the outflow of FPI impact the Indian market and the rupee? (250 Words)

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Approach / Explaination / Answer

Approach

- Give a Brief Introduction about FPI and FDI.
- Explain the difference between FDI and FPI.
- Comment on impact of FPI outflow on value of rupee and India market.

Ans

A Foreign Direct Investment (FDI) is an investment made by a firm or individual in one country into business interests located in another country. Foreign portfolio investment (FPI) consists of securities and other financial assets passively held by foreign investors. It does not provide the investor with direct ownership of financial assets and is relatively liquid depending on the volatility of the market.

Difference Between FDI and FPI:

Parameters	Foreign Direct Investment (FDI)	Foreign Portfolio Investment (FPI)
Definition	FDI refers to the investment by the foreign investors to obtain a substantial interest in enterprises located in different countries.	FPI refers to investing in financial assets of a foreign country such as stocks and bonds available on an exchange.
Role of Investors	Active Investors	Passive Investors
Type	Direct Investment	Indirect investement
Degree of control	High control	Very low control
Term	Long Term Investment	Short Term Investment
Management of Projects	Efficient	Comparatively less efficient
Investment has done on	Physical assets of the foreign country	Financial Assets of foreign Country
Entry and Exist	Difficult	Relatively Difficult.
Leads to	Transfer of funds, Technology and other resources to the	Capital inflow to the foreign country

	foreign country.	
Risks involved	Stable	Volatile

The impact of FPI outflows on the Indian market and the rupee:

- The stock markets have been rattled by persistent capital withdrawals from the capital market, which has also caused the rupee to weaken as global inflation rates rise.
- India's foreign exchange reserves will decrease mostly as a result of the strengthening dollar and FPI withdrawals.
- Due to ongoing withdrawals of foreign funds, the value of the rupee decreased in relation to the US dollar.
- Import costs may rise when the rupee falls in value. Thus rupee depreciation may lead to higher import bills.
- The market fell as a result of the global market's sensitivity to quantitative tightening.
- The depreciation of the rupee would result in higher oil import costs, which will further raise inflation.

FPI and FDI are both important sources of funding for most economies. Foreign capital can be used to develop infrastructure, set up manufacturing facilities and service hubs, and invest in other productive assets such as machinery and equipment, which contributes to economic growth and stimulates employment.