

“A STUDY ON THE IMPACT OF INSTITUTIONAL INVESTORS AND MUTUAL FUNDS ON INDIAN STOCK MARKET”

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Abstract

Mutual Fund industry is witnessing rapid growth and has huge potential for growth in the economy. With the increased savings in households, investor education programmes, and tax benefits, the earning class people are now attracted to mutual fund schemes than fixed deposits. The study analyzed the importance of mutual funds in the 21st century, by finding the relation between institutional investors and how the mutual fund industry can protect itself from the crash of stock markets when foreign investors withdraw all of a sudden. For the study, data of FII, DII and Mutual Funds are taken for a period from 2009 to 2018. The findings show that a stronger effort in financial education and literacy programmes in rural areas will make the Indian stock markets more reliable, while attracting newer participants to the Mutual Funds Industry, thereby making it immune to shocks from foreign investor behavior.

Keywords: FII, DII, Mutual Funds, funds flow

I. INTRODUCTION

In a country like India, a Capital market plays a vital role in the formation of capital. As a developing country India receives a lot of foreign investments. The foreign funds flow to capital market in the form of FII and FDI. FIIs are speculators who buy and sell shares in the market. This makes the market more liquid. FDIs are investor who invest and stays with the company for its development. They are not speculators who come in for profit. FIIs are sentimental to market information and withdraw money from the invested avenues when they see an opportunity to earn more from other markets, which causes a breakdown of the Indian stock markets. India opened its market for foreign investors in 1991, and the market is properly regulated by RBI and SEBI. FIIs, and DIIs including mutual funds plays a significant role in broadening and deepening the Indian markets. FIIs have significantly more influence on Indian markets when compared to other emerging markets.

II. MOTIVATION FOR THE STUDY

Number of FIIs getting registered with SEBI is increasing year on year, and the fund flow has also drastically increased. This makes the markets more volatile. Mutual Funds also plays a vital role in the

capital market by motivating the investors across the spectrum to take advantage of the developing economy. As FIIs were making the market more volatile, and their withdrawal makes the market go down, the only way to reduce its effect is to strengthen the DIIs. Mutual Funds are a way for strengthening the DIIs. The decision of the investors to invest in capital market is largely dependent on the secondary market moments. This study focuses on how secondary market influences the inflows and outflows of mutual funds. For this, data of FII and DII is considered and measure the impact on Mutual Fund Flows.

III. REVIEW OF LITERATURE

(Murale & Christy, 2013) established a confident relation between FIIs, Sensex, market capitalization and trading turnover. They demonstrated that about 42% of the developments in the Sensex were expected to FIIs. They contended that impact of FIIs was more than DIIs on the Sensex. This investigation considered 96 month to month perceptions and 250 day by day perceptions crossing between January 2000 and December 2007.

(Alekhya & Saritha, 2016) studied the trends and challenges of mutual fund industry. Mutual funds industry has a large scope in India, as it provides platform for small investors to invest in share markets. The advantage of mutual funds is that the funds will be managed by professional portfolio managers. The recent trend shows that there is an increase in cash inflow by mutual funds. Even though the industry has a growth year on year, lack of financial education, awareness, distribution cost, cultural bias etc.. still remains as challenges for the mutual funds industry.

(Salar, 2016) studied the role of Domestic Institutional Investors in development of Indian stock market. The author tried to find out how the sensex moves based on the buy and sell of DII. In Granger causality test he found the existence of a negative correlation between DII's flow and SENSEX. SENSEX raised as the net flows of Domestic funds got decreased and when SENSEX fall when Domestic funds net flows increases. He concluded that DII's does not have any impact on the movement of SENSEX. The trend which was seen at the study was that when DII's sell SENSEX raises and when DII's buy SENSEX falls. The study confirms that there is a negative trading behaviour between market returns and institutional flows.

(Acharya & Das, 2017) studied the perception of retail investors in mutual funds through various review studies. Mutual funds are financial intermediaries which are specialized institutions who invest in large and well diversified portfolio of securities. They create a portfolio by investing in money market instruments, bonds and share of the companies. The studies indicated that India had very much concerns on the evaluation of mutual funds. The reviews bring to attention the awareness of mutual funds among the investors of several parts of India and reasons for investing in mutual funds. The reviews also identified the

need of conducting various investor awareness programmes especially in villages and other cities were common and poor people live. They also focus on the issues like satisfactory investor protection, single regulatory authority, higher return for a given hazard according to the investor's desire, greater convenience and liquidity etc. These reviews also suggest that mutual funds should act as the agent for the growth of economy and development of the country.

(Tripathi, 2017) scrutinized the macro level determinants of FIIs flows into India for a period from January 1994 to December 2016. The study informs that there is a bi-directional causality between Net FIIs flows and the BSE Sensex. FII's are driven and drive by the market. The study also brought into light that inflow of FII leads to accumulation in foreign exchange reserves improves the creditworthiness of the country, which can influence the economic development of the country.

(Jalota, 2017) focused on the behavioural aspects of FII's and DII's the author tried to find out the existence of any behavioural reliance between FII and DII in the stock market and how it affects. The creator discovered that there is a solid negative connection. Which means that when FII sells DII buys and vice versa. India as a developing economy cannot depend on the foreign investors alone. That can weaken the economy all of a sudden when the FII's withdraw the funds from India. So the government should take necessary steps to make it attractive for FII's to stay invested in India.

(Wazal, 2017) attempted to learn the effects of trading pattern of Foreign Institutional Investors on Indian capital market. FII has huge impact on Indian economy. It showed a huge role in deciding the GDP of India. So the government welcomes foreign investments. The government lifted up the bails for the foreign institutions to invest in India. The lack of investment options in other countries, availability of resources and the easiness to invest in India, made it the most attractive for investors to invest huge amount of money. The researcher establishes that there are noteworthy fluctuations in the Indian capital market returns and volatility is expressively reduced after opening up of the market to foreign investors.

(Sathish & Srinivasan, 2018) examined the causal relationship that may exist between institutional investors and Indian stock market by using Granger causality test. The data consisted of 5 years from 2011 to 2015. CNX Nifty is taken as market representation of Indian stock market for analyzing with econometric tools. They found a 5% level of significance a unidirectional causality between Nifty and FII's gross purchase. The study provided evidence that both the institutional investors are influenced by each other's actions in the Indian stock market. The trading behaviour of FII's and DII's are opposite to each other in Indian stock market. Whenever FIIs make a buying or selling, it directly impacts the investment choice of DIIs. Moreover, when DIIs invest or withdraw from the market, it had an impact on FIIs.

(Ahuja, 2018) studied the relationship between Mutual Fund investment and BSE SENSEX. Data for 12 years from 2001 to 2012 was considered for the study. Pearson's correlation coefficient and simple

regression OLS model is used for analysis of data and studies that the mutual funds investment in stock market does not have significant impact in deciding the trends of BSE SENSEX. The correlation between mutual fund investments and SENSEX is negative.

IV. RESEARCH GAP

- No study has been conducted to know the factors affecting mutual funds.
- No research was conducted to find the impact of mutual funds on NIFTY returns

V. NEED FOR THE STUDY

Mutual funds are playing vital role in the capital markets and also motivates the investors who are not in a position to take the advantage of the economic growth. The investors make their decisions to invest based on the market movements. Institutional investors have a huge role in making the market movements than the retail investors. Foreign investors are one of the big market movers, which make the markets more volatile. Hence, it was understood that there is a need to study how the effect of FIIs can be reduced in the capital markets.

VI. METHODOLOGY

Objectives of the study

1. To study the impact of Nifty with FII and DII on Indian stock market.
2. To measure the mutual funds impact on Indian stock market.
3. To check whether the mutual fund inflow and outflow were affected by external fund flow into equity market.
4. To predict and understand the trend of mutual funds and FII

Hypothesis of the study

Ho1:- FII does not have impact on nifty returns

Ho2:- DII does not have impact on nifty returns

Ho3:- Institutional fund flow doesn't cause mutual funds inflows and outflows.

Data Collection Method

Data's relating to FII, DII, Mutual Funds and NIFTY returns is collected from RBI, SEBI, NSE and AMFI. The data is taken from the period of 2009 to 2018. The data is taken from the period of 2009 so as to study the impact after the economic recession of 2008.

VII. RESULTS AND DISCUSSION

Variable	Coefficient	Std. Error	t-Statistics	Prob.
C	1.6800008	6193091	27.14182	0.0000
FII net	44226.87	6036.901	7.326089	0.0000

Table 1.1 represents linear regression results of NIFTY on FII

R-squared	0.024794
Adjusted R-squared	.024332
Durbin –Watson	.926738

Table 1.2 represents model summary of the result

To find the impact of returns FII on NIFTY , NIFTY return is taken as dependent variable and FII as independent variable. It was found from the study that FII has a positive impact on NIFTY returns with a t-statistic value of -7.326 at 0.01 significance level. Which means, when there is an increase in the inflow of foreign investments the NIFTY returns also increases. And when there is an outflow of FII the NIFTY returns also decrease accordingly.

Variable	Coefficient	Std. Error	t-Statistics	Prob.
C	1.5700008	6117295	25.63350	0.0000
DII net	-108869.2	9206.991	-11.82462	0.0000

Table 1.3 represents linear regression results of NIFTY on DII

R-squared	0.062148
Adjusted R-squared	.061703
Durbin –Watson	1.006870

Table 1.4 represents model summary of the result

To find the impact of DII on NIFTY returns, NIFTY return is taken as dependent variable and DII as independent variable. It was found from the study that DII has a negative impact on NIFTY returns with a t-statistic value of -11.824 at 0.01 significance level. This means that even though DII make bulk investment into the market the NIFTY returns still go down.

Variable	Coefficient	Std. Error	t-Statistics	Prob.
C	-1.000000	4.420009	-2.260008	0.0000
MF Inflow	4.930016	1.380017	35.73713	0.0000

MF Outflow	1.000000	2.020017	4.960016	0.0000
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Table 1.5 represents linear regression results of NIFTY on Mutual Funds Inflow and Outflow

R- squared	1.000000
Adjusted R-squared	1.000000
Durbin - watson	1.590301

Table 1.6 represents model summary of the result

The regression test shows that NIFTY returns has an impact due to the cash flows of mutual funds. The factors, Mutual funds inflow and outflow significantly effects NIFTY returns by 4.93 and 1 respectively. In this regression test NIFTY returns was taken as the dependent variable and Mutual funds inflow and outflow as the independent variables. Durbin Watson value is below 2 which indicate that it is significant.

Variable	Coefficient	t-Statistics	Prob.
C	129.1370	7.231999	0.0000
DII	-0.944649	-35.14173	0.0000

Table 1.7 represents linear regression results of FII on DII

R- squared	0.369086
Adjusted R-squared	0.368787
Durbin - watson	1.856732

Table 1.8 represents model summary of the result

This regression test is done to determine whether there is any impact of FII on DII. The dependent variable is FII and DII is the independent variable. The result shows that FII negatively impacts DII at 0.01 level of significance. The Durbin Watson value also stands below 2, which means that it is significant.

Variable	Coefficient	t-Statistics	Prob.
C	175.9678	6.737838	0.0000
MF Inflow	-1.040007	-0.867908	0.3855
MF Outflow	-4.050007	-4.970095	0.0000

Table 1.9 represents linear regression results of FII on Mutual Funds Inflow and Outflow

R- squared	0.036032
Adjusted R-squared	0.35119
Durbin - watson	1.41.938

Table 1.10 represents model summary of the result

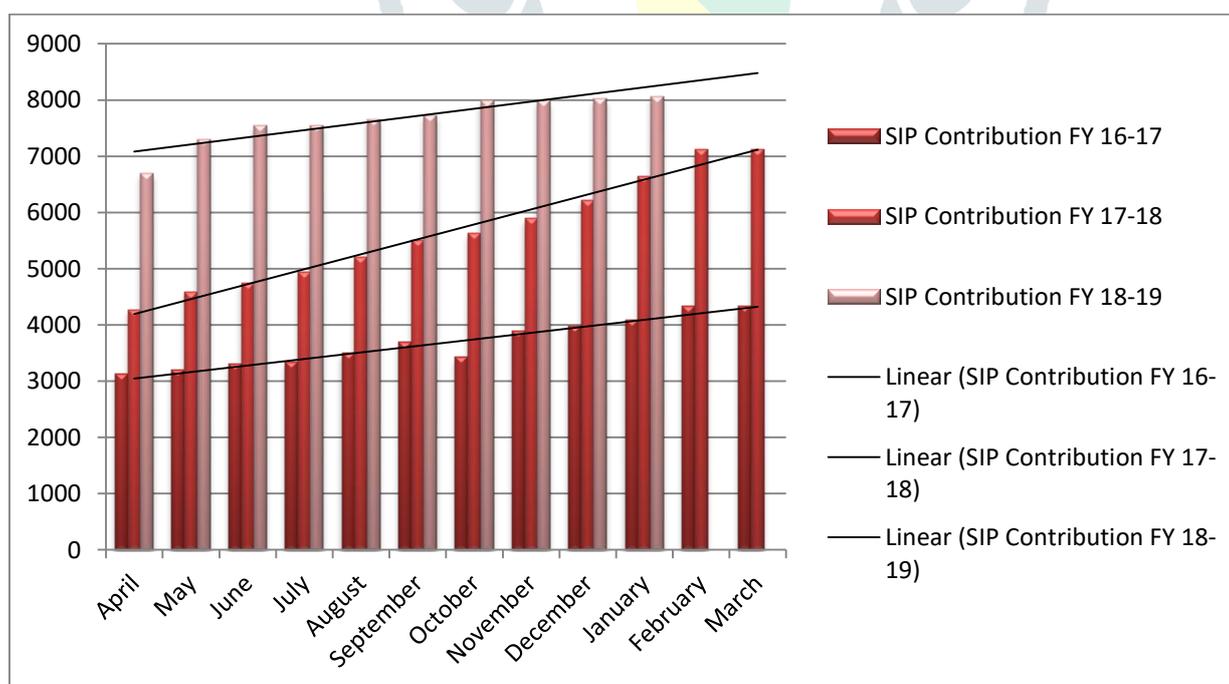
The regression test is done between FII and Mutual funds inflow and outflow. Dependent variable is FII and independent variables are Mutual funds inflow and outflow. FII does not have any impact on Mutual Funds Inflow as the significance level is more than .05. And FII has an impact with Mutual Funds outflow at 0.01 level of significance.

Null Hypothesis	F statistic	Prob
FII does not granger cause MF inflow	4.58164	0.0103
FII does not granger cause MF outflow	4.29875	0.0137
DII does not granger cause MF inflow	7.26644	0.0007
DII does not granger cause MF outflow	8.40686	0.0002

Table 1.11 represents granger causality results

To know the effect of Mutual Funds inflow and outflow on FII and DII, Granger Causality test is applied and was found that FII does not granger cause Mutual Funds inflow and outflow. In the case with DII, the investments made by domestic institutions do not cause mutual funds inflow and outflow. The test results says that FII and DII does not granger cause Mutual Fund inflow at 0.0103 and 0.0007 level of significance respectively and FII, DII does not granger cause Mutual Fund outflow at 0.0137 and 0.0002 level of significance respectively.

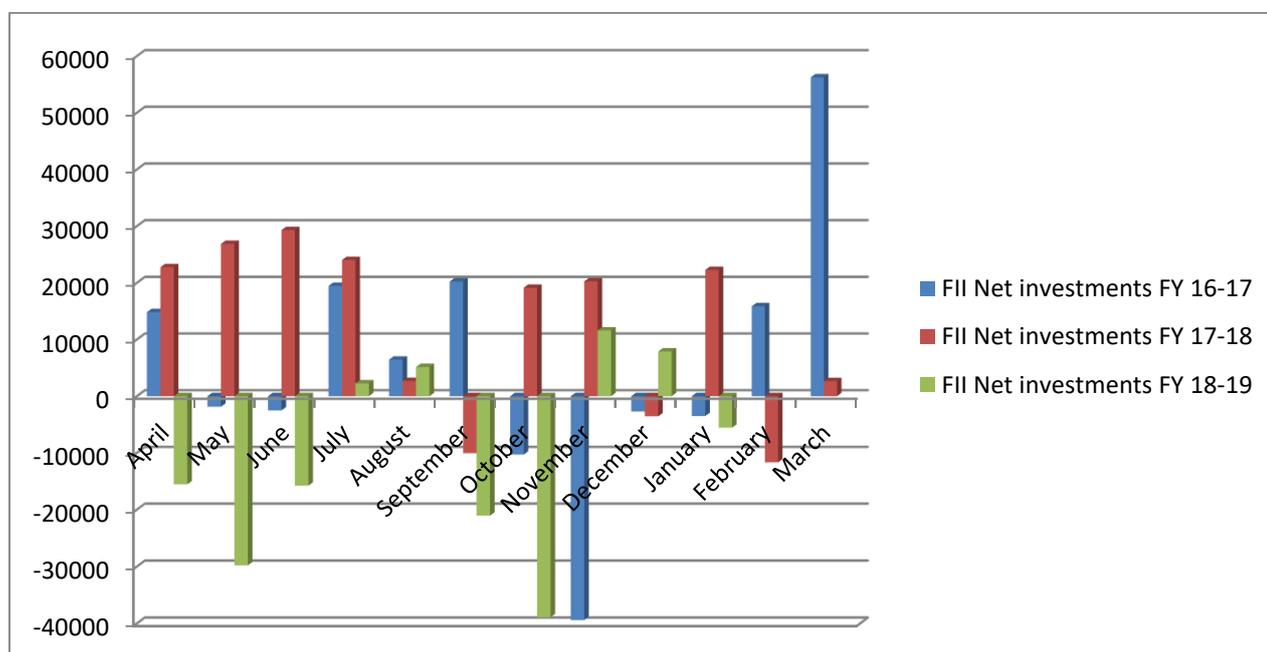
Trend analysis of SIP investments (Chart 1)



The above trend analysis of SIP investments shows that there is an increasing demand for this scheme. By the end of month of January 2019 there is currently about 2.57 crore active SIP accounts. The total

contribution during financial year 2016-17 amounts to rs. 43,921 crore and has increased to rs. 67,190 crore in financial year 2017-18 and in the current financial year still excluding the month of February and March the contribution to SIP by investors have reached rs. 76,543 crore.

Pattern analysis of FII net investment (Chart 2)



The above chart is a presentation of net FII investments made in three different financial years. We can see that in the current financial year there is downward trend in the investment of FII. The FII investment deviates causing huge market volatility. The amount represented in the graph includes equity funds, debt funds, and hybrid funds.

VII. SUMMARY AND FINDINGS

- The inflows and outflows of foreign institutional investors directly impacts the stock returns. The stock returns move along with FII. When the inflow is higher the stock return increases and when the outflow is higher stock return decreases.
- Investments made by the domestic institutional investors are higher when the foreign institutional investors withdraw from the market. They help in decreasing the effect of outflow of foreign funds. However when the investments made by the domestic institutions are high the stock returns goes down.
- The flow of mutual funds also affects the NIFTY returns.
- The regression test done for testing the impact of FII on DII states that the foreign investment has a negative relationship with the domestic investments.
- The study indicates that when the foreign outflow is higher the domestic inflow will be higher and vice versa.
- The mutual funds inflow is not influenced by the foreign institutional investments. But they do influence the outflow.

- The mutual fund data shows that creating awareness among the investors is good for the mutual fund industry as the number of mutual fund account schemes subscribed is increasing.

XI. CONCLUSION

From the data analysed for a period of 2009 to 2018 it was found that institutional investors impact the Indian stock markets. So the null hypotheses are rejected and alternative hypotheses are accepted. More investments from domestic institutional investors can make the Indian markets less volatile. The fluctuations happen in the market because of sentiments of the investors. The investors, when they see an opportunity to earn more returns from another market, especially the foreign investors, will withdraw from the current market and invest in those avenues. The mass withdrawal makes the market go down.

Mutual fund industry has huge potential in India. But the industry has not used its potential to capture the market. Even though many efforts were taken to increase the awareness among the investors it was not a huge success. More initiatives should be taken from the market players and the government to give awareness to the common people.

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