

Foreign Portfolio Investment

A foreign portfolio investment is a grouping of assets such as stocks, bonds, and cash equivalents. Portfolio investments are held directly by an investor or managed by financial professionals.

Following the presentation of the Union Budget in 2021-2022, it was reported that the Sensex showed an 11.36% increase due to Foreign Portfolio Investments in India.

This article will give details about Foreign Portfolio Investment within the context of the UPSC Exams.

Overview of Foreign Portfolio Investments

Foreign portfolio investments consist of securities and other financial assets that are held passively by a foreign investor. This does not provide the foreign investor with direct ownership of the financial asset in question.

Foreign portfolio investments can be done by individuals, companies or even government agencies. Such investments help entrepreneurs in diversifying their portfolio, giving them an edge in international markets.

An FPI will be featured in a country's capital account and is part of the balance of payments which takes stock of money flowing in and out of the country over a specific period of time.

Benefits of Foreign Portfolio Investments are as follows:

- **Portfolio diversification:** FPI enables investors to diversify their portfolios on the international stage.
- **International Credit:** FPI can give creditors a large credit base as it provides access to credit in foreign nations.
- **Benefits from the Exchange rates:** If an investor has an FPI in a foreign country with a stronger currency than their own country, the difference in exchange rates between the two countries can benefit the investor.

Foreign Portfolio Investment vs Foreign Direct Investment

In a foreign portfolio investment, it is not necessary for an investor to actively manage the investment or the companies that issue the investment. In other words, they don't have direct control over the assets.

Through foreign direct investment, an investor is allowed to purchase a direct business interest in a foreign country. For example, an investor based in Bangalore purchases a restaurant chain in Tokyo to

lease to an American company that needs space to expand its operations. The investor's goal is to create a long-term income stream while helping the company increase its profits.

This Foreign Direct Investment (FDI) investor controls their investments directly and plays an active role in deciding where the company puts the money. The investor helps in setting up the business and nurtures it to the point where he/she can ascertain there is a viable return on investment (ROI). Since the investor money is fully committed to the business, they will face liquidity and more risk when selling the interest.

A brief info about the differences between FPI and FDI is given in the table below:

Difference between Foreign Portfolio Investment and Foreign Direct Investment	
Foreign Portfolio Investment	Foreign Direct Investment
Foreign Portfolio Investment or FPI refers to the investment made in the financial assets of an enterprise, based in one country, by the foreign investors	Foreign direct investment or FDI pertains to international investment in which the investor obtains a lasting interest in an enterprise in another country
An investor is inactive	An investor is active
Indirect investments in assets are made	Direct investments in assets are made
Investments made are short term in nature	Investments made are long term in nature
FPI are volatile in nature	FDI are stable in nature.

Frequently Asked Questions about Foreign Portfolio Investments

What is the benefit of foreign portfolio investment?

Foreign portfolio investment gives investors an opportunity to engage in international diversification of portfolio assets, which in turn helps achieve a higher risk-adjusted return.

Why is FPI less risky than FDI?

In FPI the investor does not have direct control over the securities or businesses. This means that FPI tends to be more liquid and less risky than FDI.